HONGHUA GROUP LIMITED
宏華集團有限公司

(incorporated in the Cayman Islands with limited liability)

Stock Code: 196

2010
Interim Report

CONTENTS

HONGHUA GROUP LIMITED
2010 Interim Report

Financial Highlights

OPERATING RESULTS

	Six months ended 30 June **2010** RMB'000	2009 RMB'000 (restated)	Change
Revenue	**685,596**	1,196,503	(42.7%)
(Loss)/profit from operations	**(54,095)**	85,767	(163.1%)
(Loss)/profit before taxation	**(101,350)**	86,452	(217.2%)
(Loss)/profit attributable to equity shareholders of the Company	**(89,458)**	57,589	(255.3%)
Figures per share			
(Loss)/earnings per share — Basic (RMB cents)	**(2.77)**	1.79	(254.7%)
(Loss)/earnings per share — Diluted (RMB cents)	**(2.77)**	1.79	(254.7%)

FINANCIAL POSITION

	30 June 2010 RMB'000	31 December 2009 RMB'000 (restated)	Change
Total non-current assets	**1,252,639**	1,209,071	3.6%
Total current assets	**4,651,188**	5,375,375	(13.5%)
Total assets	**5,903,827**	6,584,446	(10.3%)
Total current liabilities	**1,629,357**	2,062,235	(21.0%)
Total non-current liabilities	**111,602**	262,804	(57.5%)
Total liabilities	**1,740,959**	2,325,039	(25.1%)
Total equity	**4,162,868**	4,259,407	(2.3%)

KEY FINANCIAL RATIOS

	Six months ended 30 June 2010	2009 (restated)	Change
Gross margin	**23.6%**	26.8%	(3.2%)
Net margin	**(13.0%)**	4.8%	(17.8%)
Return on average assets	**(1.4%)**	0.8%	(2.2%)
Return on average equity	**(2.2%)**	1.3%	(3.5%)

	30 June 2010	31 December 2009 (restated)	Change
Current ratio	**2.85**	2.61	0.24
Quick ratio	**1.72**	1.69	0.03
Total debts/Total assets	**15.4%**	19.7%	(4.3%)

Corporate Information

BOARD OF DIRECTORS

Executive Directors

Zhang Mi *(Chairman)*
Ren Jie
Liu Zhi

Non-executive Directors

Siegfried Meissner
Huang Dongyang

Independent Non-executive Directors

Chen Guoming
Liu Xiaofeng
Qi Daqing
Tai Kwok Leung, Alexander
Wang Li
Shi Xingquan

SECRETARY OF BOARD OF DIRECTORS

Liu Gangqiang

BOARD COMMITTEE

Audit Committee

Qi Daqing *(Committee Chairman)*
Chen Guoming
Liu Xiaofeng
Tai Kwok Leung, Alexander
Wang Li
Shi Xingquan

Corporate Governance Committee

Liu Xiaofeng *(Committee Chairman)*
Chen Guoming
Qi Daqing
Tai Kwok Leung, Alexander
Wang Li
Shi Xingquan

Remuneration Committee

Liu Xiaofeng *(Committee Chairman)*
Zhang Mi
Qi Daqing

Strategic Investment and Risk Control Committee

Zhang Mi *(Committee Chairman)*
Ren Jie
Liu Zhi
Huang Dongyang
Wang Li
Shi Xingquan

JOINT COMPANY SECRETARIES

Liu Gangqiang
Corinna Leung

QUALIFIED ACCOUNTANT

Lu Hong *(FCCA, HKICPA, CICPA)*

Corporate Information

LEGAL ADVISORS

as to Hong Kong law

King & Wood

as to Cayman Islands law

Appleby

PRINCIPAL BANKERS

Bank of China Limited
Agricultural Bank of China
China Merchants Bank Co., Ltd
Industrial and Commercial Bank of China Limited
China Construction Bank Corporation
The Hongkong and Shanghai Banking
Corporation Limited
The Export-Import Bank of China
JPMorgan Chase Bank (China) Company Limited

AUDITOR

KPMG
Certified Public Accountants

COMPLIANCE ADVISER

CCB International Capital Limited

REGISTERED OFFICE

Clifton House
75 Fort Street, PO Box 1350
Grand Cayman, KY1-1108
Cayman Islands

HEAD OFFICE

99 East Road, Information Park,
Jinniu District
Chengdu, Sichuan 610036
PRC

PLACE OF BUSINESS IN HONG KONG

Room 2508, Harcourt House
39 Gloucester Road
Wan Chai
Hong Kong

PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Appleby Trust (Cayman) Ltd.
Clifton House
75 Fort Street, PO Box 1350
Grand Cayman, KY1-1108
Cayman Islands

HONG KONG BRANCH SHARE REGISTRAR AND TANSFER OFFICE

Computershare Hong Kong
Investor Services Limited
Shops 1712–1716
17th Floor Hopewell Centre
183 Queen's Road East
Wanchai
Hong Kong

STOCK CODE

The Stock Exchange of Hong Kong Limited: 0196

WEBSITE:

http://www.hh-gltd.com

MANAGEMENT DISCUSSION AND ANALYSIS

Management Discussion and Analysis

During the six months ended 30 June 2010 (the "Period"), the Group recorded a turnover of approximately RMB686 million, a decrease of 42.7% as compared to RMB1,197 million recorded during the six months ended 30 June 2009 (the same period last year). Gross profit was RMB162 million and loss attributable to equity shareholders of the Company was RMB89 million.

INDUSTRY REVIEW

Although the global economy showed signs of recovery in the first half of 2010, the pace of recovery was relatively slow, especially the U.S. and China where the economic growth rates were lower than market anticipation. Furthermore, the European debt crisis caused a decrease in demand for oil, leading to fluctuation in world crude oil prices. As a result, the steady recovery of global drilling activities and drilling rig day rates were restrained. During the Period, global drilling activities recorded a slight increase amid volatility. According to Schlumberger research, there were 4,788 units of active drilling rigs worldwide as at the end of June 2010, representing an increase of only 6% as compared to the beginning of the year. In regards to the geographical distribution, apart from North America recording an increase in land drilling activities as compared to the same period last year, the utilization rates of land and offshore drilling equipment in other regions were still as low as those in 2009. In April 2010, the largest oil spill ever in American history occurred in the Gulf of Mexico. In the short-term, the incident will undoubtedly restrain the rebound in offshore drilling activities and fleet utilization rates. From a long-term perspective, however, the incident will greatly arouse concerns about the safety standards of drilling platforms, triggering a new round of equipment replacement which favors the

DC drilling motor

offshore drilling equipment industry. Furthermore, large international energy enterprises, such as Shell and Exxon Mobil Oil have been deploying their new unconventional gas business. In addition, the PRC government has implemented a number of favorable policies and incentive schemes in unconventional natural gas exploration, bringing new business opportunities to the related drilling equipment industry.

PRODUCTION, RESEARCH AND DEVELOPMENT

Although the sales volume of land drilling rigs was affected by the macro economic downturn and the slow recovery of the global land rig market during the Period, the Group implemented initiatives for enhancing productivity and facilitating operational capability steadily in order to capture potential opportunities arising from the revival of the global economy and land rig market. Currently, the Group is engaged in the construction of its new Jiangsu Qidong offshore manufacturing base. The new motor plant and production line of the Group's Guanghan production base is completed and will commence operations in the near future. The Group's U.S. assembly base has already been operating on the assembly and refurbishment business for domestic U.S. clients, while the Group's drilling rig parts and components distribution center in Irkutsk, Russia has also begun operations. In addition, the Group utilized the ERP system for further enhancement of production process, reduction in production costs, strict cost control, and further strengthening of supplies and materials management. Regarding quality control, the Group strictly abides by the requirements of APIQ1 8th Edition and ISO9001 and constantly modifies and optimizes the quality control system to be stricter and more professional for all procedures ranging from raw materials purchase, production to final product testing. The Group's quality control system also gradually extends from the self-manufacturing sector to external co-production and outsourcing sectors to ensure that the Group's final products conform to the related quality standards and requirements.

40DBS Training Rig

During the Period, the Group continued to strengthen the design, research and development of its products, so as to adapt to different drilling conditions, meet the demand of different markets and maintain its leading position in the market. The Group completed the design of new super single pipe rigs and conducted trial production of coiled tubing rigs, which will be promoted in the market soon. The design of the first "Honghua No. 1" jack-up rig has been completed and submitted to the American Bureau of Shipping ("ABS") for review, and is expected to be approved in the near future. To satisfy the needs of various markets in fast moving rigs, the Group successfully developed a series of skidding devices, including the new desert trailer drilling rigs sold to Kuwait, the train-skidding device successfully promoted in the Russian market, as well as the hydraulic step-by-step skidding system applied to cluster wells and new vehicular rigs designed for the North American market. In addition, the Group remained

BAPEX ZJ70DBS Rig Delivery Ceremony

committed to developing high value-added parts and components, such as Quintuple motor direct drive pump, offshore drilling platforms and drilling modules applied to offshore drilling rigs.

As at 30 June 2010, the Group has a total of 364 research and development personnel. The total research and development expenses amounted to RMB19 million, representing an increase of 25.1% as compared to the same period last year. Meanwhile, the Group is planning to establish an offshore equipment research centre in Shanghai, fully utilizing high-quality local technology and human resources in order to build a solid foundation for penetrating into the offshore drilling and exploration market. During the Period, the Group had 29 new patent applications and 11 of them were new inventions. The Group has accumulated applications for up to 72 patents (41 of them are pending for the approval of the Chinese State Intellectual Property Office).

PROSPECTS

The Group takes a cautious view of its business for the second half of 2010. It is predicted that the depressed market will still pose serious challenges for the Group's business. However, the Group continues to believe that the development of the global economy in the foreseeable future will still rely on oil and natural gas resources. In the long run, expenditure on oil and gas exploration and production will continue to increase significantly. Oil and gas resources and the related equipment industry will certainly ride out the market cyclical downturn. Therefore, the Group is well prepared for potential opportunities and development. We will continue to focus on the design and production of high-efficiency and high-quality land and offshore drilling equipment. We will also further penetrate into Central Asia and Russia in terms of our new business of oil and gas engineering services. Meanwhile, we will capture the business opportunities arising from the sustaining

Assemble the mud pump

development of the unconventional natural gas market such as shale gas and coalbed methane, by developing a series of products for the exploration of unconventional gas, as well as searching for potential cooperative development projects.

The Group believes that leveraging on the strengths of manufacturing land and offshore oil and gas equipment, it will gradually extend its production chain to realize vertical and horizontal expansion and become a strong and competitive participant in the industry. Having encountered the challenges of economic and cyclical industry downturn, by relying on continuous practice and accumulation of experience, the Group will gradually transform into a diversified energy company with interactive development in the fields of equipment production, resource exploration and engineering services based on the solid experience on land and offshore oil and gas equipment manufacturing.

70DBS Rig

FINANCIAL REVIEW

During the Period, the Group's gross profit and loss attributable to equity shareholders of the Company amounted to approximately RMB162 million and RMB89 million respectively. Gross margin and net loss margin amounted to approximately 23.6% and 13.0% respectively. During the Period, the decrease of the Group's gross profit and loss attributable to shareholders was mainly due to the substantial decline in the Group's total turnover which was caused by the prolonged influence of the financial crisis and slow recovery in oil demand.

Revenue

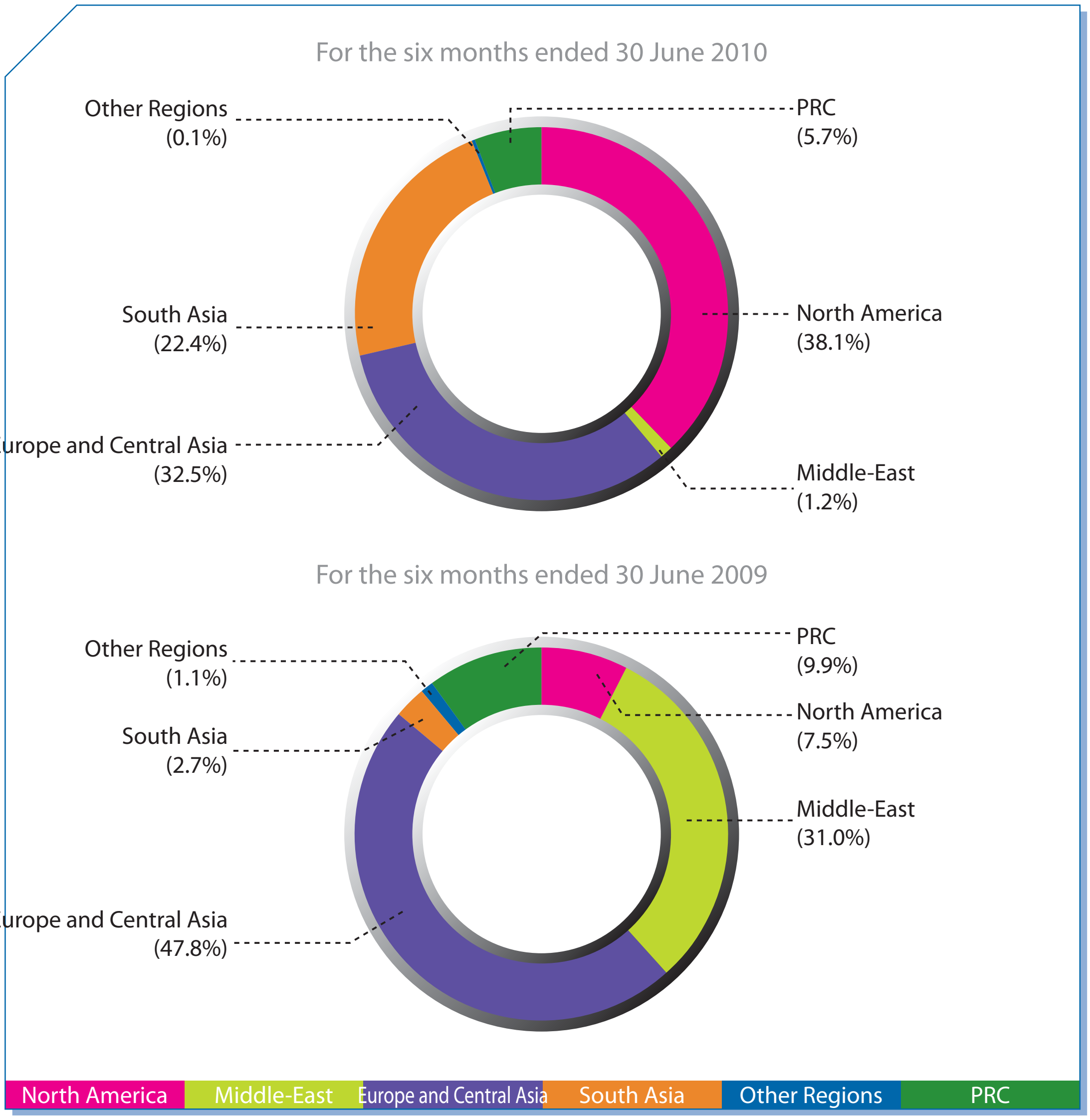
During the Period, the Group's revenue amounted to approximately RMB686 million, representing a decrease of approximately RMB511 million or 42.7% as compared to approximately RMB1,197 million in the same period last year. The decrease in revenue was mainly attributable to the slow recovery of the global land rig market which led to the weakened demand for land rigs. During the Period, total number of rigs sold decreased to 9 units from 27 units in the same period last year.

During the Period, revenue from exports amounted to approximately RMB647 million, representing a decrease of RMB431 million as compared to the same period last year, and accounted for approximately 94.3% of the Group's total revenue. Among which, revenue from the European and Central Asian markets, and Middle-Eastern market decreased significantly due to slowdown in demand. During the Period, the sales volume of the said markets decreased to 3 and 0 units respectively from 14 and 6 units respectively in the same period last year. The North American market recovered gradually and a sales volume of 3 units was recorded, as compared to 1 unit in

Fund management company's visit to Honghua

the same period last year. During the Period, the South Asian market was penetrated and a 70DBS rig with high configuration requirements was sold to the People's Republic of Bangladesh, while only 3 units with low configuration requirements were sold in the same period of last year. Meanwhile, the Group's revenue in the PRC market and other areas experienced different degrees of decrease, among which, the sales volume of rigs to the PRC was 2 units, as compared to 3 units in the same period last year.

Revenue by Geographical Areas



During the Period, revenue by product categories was as follows:

Revenue by product categories	For the six months ended 30 June 2010 Revenue (RMB'000)	Proportion (%)	Quantity (unit)	For the six months ended 30 June 2009 Revenue (RMB'000)	Proportion (%)	Quantity (unit)	2010.1-6 vs 2009.1-6 Change (RMB'000)	Change (%)
Digitally-controlled Rigs	**466,642**	**68.1%**	**9**	759,574	63.5%	19	**(292,932)**	**-38.6%**
Conventional Rigs	**–**	**–**	**–**	264,125	22.1%	8	**(264,125)**	**-100.0%**
Subtotal	**466,642**	**68.1%**	**9**	1,023,699	85.6%	27	**(557,057)**	**-54.4%**
Mud Pumps	**60,111**	**8.8%**	**55**	71,072	5.9%	64	**(10,961)**	**-15.4%**
Other Parts and Components	**158,843**	**23.1%**		101,732	8.5%		**57,111**	**56.1%**
Subtotal	**218,954**	**31.9%**	**55**	172,804	14.4%	64	**46,150**	**26.7%**
Total	**685,596**	**100.0%**		1,196,503	100.0%		**(510,907)**	**-42.7%**

During the Period, revenue from drilling rigs as well as parts and components were RMB467 million and RMB219 million respectively, representing a decrease of 54.4% and an increase of 26.7% as compared to RMB1,024 million and RMB173 million in the same period last year.

Drilling rigs comprise of digitally-controlled land rigs and conventional land rigs. During the Period, all the rigs sold were digitally-controlled rigs, revenue from which amounted to RMB467 million. The decrease in revenue from drilling rigs was mainly due to the decrease in sales volume of drilling rigs from 27 units in the same period last year to 9 units during the Period. Meanwhile, increased drilling rig configuration requirements caused the average price to rise to RMB52 million during the Period, up from RMB38 million in the same period last year. During the Period, the Group recorded sales of 2 heavy 7000-meter drilling rigs, 4 medium 5000-meter drilling rigs, 2 medium 4000-meter drilling rigs and 1 light 1000-meter drilling rig.

The increase in revenue from parts and components was mainly due to sales of 5 train-skidding rig device with a sales amount of RMB65 million, compared to zero in the same period last year. During the Period, sales of 55 units of mud pumps was recorded, among which, 9 were mud pumps with high configuration requirements, as compared to 64 units and 8 units respectively in the same period last year.

Cost of Sales

During the Period, the Group's cost of sales amounted to approximately RMB524 million, representing a decrease of approximately RMB352 million or 40.2% as compared to the same period last year. The decrease was mainly due to the decrease in the Group's revenue.

Gross Profit and Gross Margin

During the Period, the Group's gross profit recorded approximately RMB162 million, representing a decrease of RMB159 million as compared to the same period last year, among which, gross profit from digitally-controlled rigs amounted to approximately RMB97 million, representing a decrease of 51.3% as compared to the same period last year. No sales of conventional rigs were recorded during the Period. Gross profit from parts and components amounted to approximately RMB64 million, representing an increase of 38.1% as compared to the same period last year.

During the Period, the Group's overall gross margin was 23.6%, representing a decrease of 3.2 percentage points as compared to 26.8% in the same period last year.

The gross margin for drilling rigs was approximately 20.8%, representing a decrease of 6.0 percentage points as compared to 26.8% in the same period last year. The decline in margin was mainly due to the special offers for clients because of weakened market demand and relatively low gross margin gained in carrying trade of part of the components.

Gross margin of rig parts and components was 29.4%, representing an increase of 2.4 percentage points as compared to the same period last year. Among which, gross margin of mud pumps was 38.5%, representing an increase of 13.6 percentage points as compared to 24.9% in the same period last year. The increase in margin was mainly attributable to the rebound of North American market. Sales of mud pumps fabricated by the Group's US plant over the total sales of mud pumps has increased to 96.7% from 48.9% compared to the same period last year, and exports have relatively higher gross margin. The gross margin of other rig parts and components was 26.0%, representing a decrease of 2.5 percentage points as compared to 28.5% in the same period last year.

Other Net Operating Revenue and Other Net Income

During the Period, the Group's other net operating revenue amounted to approximately RMB1.97 million, representing an increase of approximately RMB1.5 million, or 320% as compared to RMB0.47 million in the same period last year. The increase was mainly due to increase in revenue of services provides to overseas customers. Other net income amounted to approximately RMB1.25 million, representing a decrease of RMB3.11 million or 71.3% as compared to RMB4.36 million in the same period last year. The decrease was mainly due to the decrease in subsidy income.

Expenses in the Period

During the Period, the Group's selling expenses amounted to approximately RMB70 million, representing a decrease of RMB42 million or 37.4% as compared to RMB112 million in the same period last year. The decrease was mainly attributable to a reduction in transportation cost to RMB24 million, representing a decrease of 61.9% as compared to RMB62 million in the same period last year, and a reduction of agency fee to RMB14 million, representing a decrease of 24.9% as compared to RMB20 million in the same period last year. During the Period, the decrease in transportation cost was mainly due to the decrease in sales volume.

During the Period, the Group's general and administration expenses amounted to approximately RMB149 million, representing an increase of RMB21 million or 16.3% as compared to RMB128 million in the same period last year. The increase was mainly due to an increase in research and development expenses of RMB4 million and a consultation fee of RMB4 million during the Period. Meanwhile, the depreciation and staff cost increased by RMB3 million and RMB2 million respectively as compared to the same period last year.

During the Period, the Group's net finance expense amounted to approximately RMB46 million, as compared to net finance income of RMB3 million in the same period last year. The significant increase in net finance expenses was mainly attributable to a net exchange loss of RMB31 million in the Group's related contracts due to the relatively significant decrease in the exchange rate of the Euro against RMB, compared to a net exchange gain of RMB21 million from the exchange gain of contracts in the Euros and US dollars in the same period last year.

Share of Loss from Jointly Controlled Entities

During the Period, the Group's share of loss from jointly controlled entities amounted to approximately RMB1 million, representing a decrease of RMB1 million as compared to share of loss of RMB2 million in the same period last year.

Loss/Profit before Taxation

During the Period, loss before taxation of the Group amounted to approximately RMB101 million, whereas profit before taxation was RMB86 million in the same period last year. The loss was mainly attributable to the sharp decrease in gross profit.

Income Tax Credit/expenses

During the Period, the Group's income tax credit amounted to approximately RMB12 million, as compared to the income tax expense of approximately RMB20 million in the same period last year. The decrease was mainly attributable to the loss before taxation.

Loss/Profit for the Period

During the Period, the Group's loss amounted to approximately RMB89 million, as compared to a profit of approximately RMB66 million in the same period last year. Among which, loss attributable to equity shareholders of the Company was approximately RMB89 million, while loss attributable to non-controlling interest was approximately RMB0.28 million. Net loss margin was 13.0%, as compared to a net profit margin of 4.8% in the same period last year, which was mainly attributable to the decrease in gross profit and a higher general and administration cost rate.

Earnings before Interest, Taxes, Depreciation and Amortization ("EBITDA") and EBITDA Margin

During the Period, EBITDA loss amounted to RMB13 million, as compared to an EBITDA of approximately RMB123 million in the same period last year. The loss was mainly due to the decrease in gross profit. The EBITDA loss margin was 1.8%, as compared to a margin of 10.4% in the same period last year, which was mainly attributable to the decrease in gross profit and a higher general and administration cost rate.

Dividend

For the six months ended 30 June 2010, the Board does not recommend the payment of interim dividend.

Source of Capital and Borrowings

The Group's principal sources of capital include listing proceeds, cash from operations and bank borrowings.

Management Discussion and Analysis

As at 30 June 2010, the Group's bank borrowings amounted to approximately RMB908 million, representing a decrease of approximately RMB391 million as compared to 31 December 2009. Among which, borrowings repayable within one year amounted to approximately RMB805 million, representing a decrease of RMB241 million as compared to 31 December 2009.

Deposit and Cash Flow

As at 30 June 2010, the Group's cash and cash equivalents amounted to approximately RMB1,541 million, representing a decrease of approximately RMB62 million as compared to 31 December 2009.

During the Period, the Group's operating cash inflow amounted to approximately RMB9 million, cash inflow from investing activities amounting to approximately RMB346 million as a result of transferral of time deposits to cash and cash equivalents, and cash outflow from financing activities of approximately RMB412 million as a result of payments of bank loans.

Assets Structure and Changes Thereof

As at 30 June 2010, the Group's total assets amounted to approximately RMB5,904 million, representing a decrease of RMB681 million, or approximately 10.3%, as compared to 31 December 2009. Among which, current assets amounted to approximately RMB4,651 million, which were mainly listing proceeds, inventories and trade receivables and accounted for approximately 78.8% of total assets; non-current assets amounted to approximately RMB1,253 million, accounting for approximately 21.2% of total assets.

Liabilities

As at 30 June 2010, the Group's total liabilities amounted to approximately RMB1,741 million, representing a decrease of approximately RMB584 million as compared to 31 December 2009. Among which, current liabilities amounted to approximately RMB1,629 million, accounting for approximately 93.6% of total liabilities; non-current liabilities amounted to approximately RMB112 million, accounting for approximately 6.4% of total liabilities. As at 30 June 2010, the Group's gearing ratio is approximately 29.5%, decreased by 5.8 percentage points compared to 31 December 2009.

Total Equity

As at 30 June 2010, total equity amounted to RMB4,163 million, representing a decrease of RMB97 million as compared to 31 December 2009. Total equity attributable to equity shareholders of the Company amounted to approximately RMB4,068 million, representing a decrease of RMB97 million as compared to 31 December 2009. Non-controlling interests totaled approximately RMB95 million, representing an increase of RMB0.30 million as compared to 31 December 2009. Net asset value reached approximately RMB1.29 per share, representing a decrease of RMB0.03 as compared to RMB1.32 at 31 December 2009. During the Period, the Group's loss per share was approximately RMB2.77 cents, representing a decrease of RMB4.56 cents as compared to earnings per share of RMB1.79 cents in the corresponding period last year.

Contingent Liabilities and Pledge

As at 30 June 2010, details the Group's contingent liabilities are set out in note 20 to the interim financial report.

The Group has pledged bank deposits of approximately RMB48 million, representing a increase of approximately RMB17 million as compared to 31 December 2009, in order to reduce finance cost for internally guaranteed loans.

Capital Expenditure, Major Investment and Capital Commitments

During the Period, capital expenditure of the Group on infrastructure and technical improvements amounted to approximately RMB75 million, representing an increase of approximately RMB29 million as compared to the same period last year. This was mainly due to the gradual development of offshore construction projects.

As at 30 June 2010, the Group had capital commitments of approximately RMB1,993 million, which will be used for the construction of Jiangsu Qidong offshore manufacturing base to expand the Group's business as well as its production capacity.

Foreign Currency Risk

The Group has certain foreign currency deposits. As at 30 June 2010, the Group's foreign currency deposits were equivalent to approximately RMB118 million trade receivables and other receivables denominated in foreign currency were equivalent to approximately RMB504 million. Exports and foreign currencies settled business also exposed the Group to exchange risk.

Use of Proceeds from the Initial Public Offerings

The net proceeds after the deduction of the related expenses from the initial public offering were approximately HK$2,958 million. The Group has used the net proceeds obtained from the initial public offering in accordance with the "Use of Proceeds" in the prospectus of the Company issued at 25 February 2008. As at 30 June 2010, the use of the net proceeds was as follows: proceeds of HK$1,275 million to be used for the offshore project, among which HK$339 million was incurred; proceeds of HK$592 million to be used for potential acquisitions, none has incurred; proceeds of HK$354 million to be used for production capacity expansion and research and development expenses, all has incurred; proceeds of HK$737 million to be used as working capital and day to day expenses, all has incurred.

Employee Remuneration and Benefit

During the Period, the average number of the Group's employees was 3,401. The total remuneration and benefit amounted to approximately RMB137 million, representing an increase of RMB18 million or approximately 15.4% as compared to the same period last year. It was mainly attributable to the offshore research and development in oil and gas drilling market began from the second half of 2009, incurring a labor cost of RMB8 million, whereas none had incurred in the same period last year. Meanwhile, the staff cost for workers on product line increased RMB7 million as compared to the same period last year.

The Group strives to maintain its outstanding corporate culture and implement a people-oriented principle. We emphasize on strengthening team cohesion and raising staff morale. To create and enhance its human resource management system which is in line with strategic plans, the Group has steadily executed the ERP project to consolidate the fundamental management and streamline operation procedures. In order to establish a competitive and fair remuneration system, the Group carried out a reform in its remuneration system during the Period, so as to standardize and enhance the remuneration system of its subsidiaries. During the Period, the Group offered training and skill enhancement programs to employees at all management levels as well as technicians in order to consolidate its workforce foundation.

Corporate Governance Report

1. OVERVIEW OF CORPORATE GOVERNANCE

The Group is committed to achieving high standards of corporate governance to safeguard the interests of shareholders and to enhancing corporate value and accountability.

The Group strives to attain and maintain high standards of corporate governance to enhance shareholder value and safeguard shareholder interests. The Group's corporate governance principles emphasize a quality Board, effective internal control and accountability to shareholders.

The Company has applied the principles as set out in the Code on Corporate Governance Practices ("CG Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Stock Exchange") ("Listing Rules").

2. CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has complied with most of the code provisions as set out in the CG Code throughout the six months ended 30 June 2010 except the vesting of roles of both Chairman and President (Chief Executive Officer).

3. CHAIRMAN AND CHIEF EXECUTIVE OFFICER

CG Code provision A.2.1 stipulates that the roles of Chairman and Chief Executive Officer should be separate and should not be performed by the same individual.

Mr. Zhang Mi is the Chairman and President (Chief Executive Officer) of the Company. He is one of the founders of the Group and possesses with knowledge and experience of the industry and the related industries. The Board believes that vesting the roles of both Chairman and President (Chief Executive Officer) in Mr. Zhang Mi provides the Company with strong and consistent leadership and allows for effective and efficient planning and implementation of business decisions and strategies.

The Board is of the view that it is in the best interests of the Group to have the 2 roles performed by Mr. Zhang Mi so that the Board can have the benefit of a chairman who is knowledgeable about the business of the Group and is most capable to guide discussions and brief the Board in a timely manner on pertinent issues and developments to facilitate open dialogue between the Board and the management.

The Company will continue to review the effectiveness of the Group's corporate governance structure and consider whether any changes, including the separation of roles of Chairman and President (Chief Executive Officer) are necessary.

4. MODEL CODE FOR SECURITIES TRANSACTIONS

The Company has adopted its own code of conduct regarding dealings of Directors and relevant employees in the Company's securities (the "Company's Code") on terms no less exacting than the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 to the Listing Rules.

Specific enquiry has been made of all the Directors and the Directors have confirmed that they have complied with both the Company's Code and the Model Code throughout the reporting period for the six months ended 30 June 2010.

No incident of non-compliance of the Company's Code by the employees was noted by the Company.

5. INDEPENDENT NON-EXECUTIVE DIRECTORS

The Board of Directors has been, at any time, in compliance with Rule 3.10(1) of the Listing Rules, which requires a company to maintain at least three Independent Non-executive Directors in the Board, and with Rule 3.10(2) of the Listing Rules, which requires one of those Independent Non-executive Directors to be specialized in accounting or relevant financial management.

6. AUDIT COMMITTEE

The Company has established an audit committee (the "Audit Committee") in compliance with the Rules 3.21 and 3.22 of the Listing Rules. The primary duties of the Audit Committee are to review and supervise the financial reporting process and internal control system of the Company and provide advice and comments to the Board.

The Audit Committee comprises all the six Independent Non-executive Directors, namely Qi Daqing (Chairman), Liu Xiaofeng, Chen Guoming, Wang Li, Tai Kwok Leung Alexander and Shi Xingquan including three Independent Non-executive Directors with the appropriate professional qualifications and accounting and related financial management expertise. Liu Yinchun was also a member of the Audit Committee and has resigned with effect from 14 April 2010.

The Audit Committee has reviewed the unaudited financial reports for the six months ended 30 June 2010 of the Company and the Group.

Report of the Board

The Board of the Company is to present its reviewed interim report for the six months ended 30 June 2010.

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS AND/OR SHORT POSITIONS IN THE SHARES AND UNDERLYING SHARES OF THE COMPANY OR ANY ASSOCIATED CORPORATION

At 30 June 2010, the interests and short positions of each Director and Chief Executive in the Shares and underlying Shares of the Company and its associated corporations (within the meaning of the Securities and Futures Ordinance ("SFO")), as recorded in the register required to be kept by the Company under Section 352 of Part XV of the SFO or as notified to the Company and the Stock Exchange pursuant to the Model Code contained in Appendix 10 to the Listing Rules were as follows:

a) Ordinary shares of HK$0.1 each of the Company

	Long/Short position	Nature of interest	Number of shares held	% of the issued share capital of the Company
Mr. Zhang Mi	Long	Personal interest, corporate interest and settlor of a discretionary trust	1,576,598,037[(1)(4)]	48.90%
Mr. Ren Jie	Long	Personal interest, corporate interest and settlor of a discretionary trust	1,576,598,037[(2)(4)]	48.90%
Mr. Liu Zhi	Long	Corporate interest and settlor of a discretionary trust	1,576,598,037[(3)(4)]	48.90%

(1) Zhang Mi individually owns 280,000 Shares. Zhang Mi is a member of the Concert Group. He is the settlor of a discretionary trust, The ZYL Family Trust, whose trustee, through Wealth Afflux Limited, holds the entire issued share capital of Ally Smooth Investments Limited, which in turn is the beneficial owner of 36% of the issued share capital of Ample Chance International Limited, which in turn is the beneficial owner of the entire issued share capital of Ally Giant Limited which holds 1,337,727,837 Shares. The Trustee of The ZYL Family Trust owns 103,800,000 Shares. Ren Jie, another member of the Concert Group and the settlor of a discretionary trust, The RJDJ Victory Trust, individually owns 169,000 Shares. The Trustee of The RJDJ Victory Trust owns 23,103,200 Shares. The Trustee of a discretionary trust, The LZWM Family Trust, whose settlor is Liu Zhi, another member of the Concert Group, owns 16,750,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 12,341,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose

settlor is Zuo Huixian, another member of the Concert Group, owns 12,244,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, owns 11,796,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 10,452,400 Shares. The other members of the Concert Group totally own 47,933,800 Shares.

(2) Ren Jie individually owns 169,000 Shares. Ren Jie is a member of the Concert Group. He is the settlor of a discretionary trust, The RJDJ Victory Trust, whose trustee, through Mowbray Worldwide Limited, holds approximately 41.34% of the issued share capital of Charm Moral International Limited, which in turn is the beneficial owner of approximately 19.09% of the issued share capital of Ample Chance International Limited, which in turn is the beneficial owner of the entire issued share capital of Ally Giant Limited which holds 1,337,727,837 Shares. The Trustee of The RJDJ Victory Trust owns 23,103,200 Shares. Zhang Mi, another member of the Concert Group and the settlor of a discretionary trust, The ZYL Family Trust, individually owns 280,000 Shares. The Trustee of The ZYL Family Trust owns 103,800,000 Shares.

The Trustee of a discretionary trust, The LZWM Family Trust, whose settlor is Liu Zhi, another member of the Concert Group, owns 16,750,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 12,341,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose settlor is Zuo Huixian, another member of the Concert Group, owns 12,244,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, owns 11,796,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 10,452,400 Shares. The other members of the Concert Group totally own 47,933,800 Shares.

(3) Liu Zhi is a member of the Concert Group. He is the settlor of a discretionary trust, The LZWM Family Trust, whose trustee, through Ecotech Enterprises Corporation, holds approximately 29.33% of the issued share capital of Charm Moral International Limited, which in turn is the beneficial owner of approximately 19.09% of the issued share capital of Ample Chance International Limited, which in turn is the beneficial owner of the entire issued share capital of Ally Giant Limited which holds 1,337,727,837 Shares. The Trustee of The LZWM Family Trust owns 16,750,000 Shares.

Zhang Mi and Ren Jie, the other two members of the Concert Group, collectively hold 449,000 Shares. The Trustees of the two discretionary trusts, whose settlors are Zhang Mi and Ren Jie respectively, collectively own 126,903,200 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 12,341,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose settlor is Zuo Huixian, another member of the Concert Group, owns 12,244,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, owns 11,796,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 10,452,400 Shares. The other members of the Concert Group totally own 47,933,800 Shares.

(4) The Concert Group is defined in the prospectus of the Company dated 25 February 2008.

b) **Share options of the Company**

	Long/Short position	Number of options held — Personal interest	Number of options held — Interest of the Concert Group
Mr. Zhang Mi	Long	13,837,000	26,353,000
Mr. Ren Jie	Long	5,687,000	34,503,000
Mr. Liu Zhi	Long	5,173,000	35,017,000
Mr. Qi Daqing	Long	1,000,000	—
Mr. Liu Xiaofeng	Long	1,000,000	—
Mr. Tai Kwok Leung, Alexander	Long	850,000	—
Mr. Liu Yinchun (Resigned as an Independent Non-Executive Director with effect on 14 April 2010)	Long	750,000	—
Mr. Chen Guoming	Long	750,000	—
Mr. Wang Li	Long	750,000	—
Mr. Shi Xingquan	Long	750,000	—

Saved as disclosed above, on 30 June 2010, none of the Directors and Chief Executives (including their spouse and children under 18 years of age) had any interest in, or had been granted, or exercised, any rights to subscribe for shares (or warrants or debentures, if applicable) of the Company and its associated corporations required to be disclosed pursuant to the SFO.

SUBSTANTIAL SHAREHOLDERS' INTERESTS OR/AND SHORT POSITIONS IN THE SHARES AND UNDERLYING SHARES OF THE COMPANY

The register of substantial shareholders required to be kept under section 336 of Part XV of the SFO shows that, at 30 June 2010, the Company had been notified of the following substantial shareholders' interests and short positions, being 5% or more of the Company's issued share capital. These interests are in addition to those disclosed above in respect of the Directors and Chief Executives of the Company.

		Number of shares held						
		Personal interest						
Name	Long/Short position	Share option	Shares interest	Corporate interest	Corporate interest and settlor of a discretionary trust	Interest of the Concert Group	Total	% of the issued share capital of the Company
Ally Giant Limited	Long	–	1,337,727,837	–	–	279,060,200	1,616,788,037[1]	50.15%
Ample Chance International Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[2]	50.15%
Wealth Afflux Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[3]	50.15%
Ally Smooth Investments Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[3]	50.15%
Equity Trustee Limited	Long	–	–	–	1,555,081,237	–	1,555,081,237[3] [5][6][9][10][14][20][22]	48.24%
Charm Moral International Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[4]	50.15%
Mowbray Worldwide Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[5]	50.15%
Ecotech Enterprises Corporation	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[6]	50.15%
Mr. Zheng Yong	Long	2,085,000	15,680,000	1,337,727,837	–	261,295,200	1,616,788,037[7]	50.15%
Beauty Clear Holdings Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[8]	50.15%
Mr. Zuo Huixian	Long	1,734,000	–	–	1,349,972,237	265,081,800	1,616,788,037[9]	50.15%
Vast & Fast Corporation	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[9]	50.15%
Mr. Zhang Xu	Long	1,833,000	–	–	1,349,524,237	265,430,800	1,616,788,037[10]	50.15%
Cavendish Global Corporation	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[10]	50.15%
Elegant Scene International Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[11]	50.15%
Mr. Wang Jiangyang	Long	941,000	4,772,600	1,337,727,837	–	273,346,600	1,616,788,037[11]	50.15%
Mr. Chen Jun	Long	872,000	2,640,400	1,337,727,837	–	275,547,800	1,616,788,037[12]	50.15%
Believe Power International Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[13]	50.15%
Mr. Fan Bing	Long	1,744,000	–	–	1,350,068,837	264,975,200	1,616,788,037[14]	50.15%
Brondesbury Enterprises Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[14]	50.15%
Mr. Zhang Yanyong	Long	1,480,000	10,479,600	1,337,727,837	–	267,100,600	1,616,788,037[15]	50.15%
Mr. Ao Pei	Long	683,000	1,968,400	1,337,727,837	–	276,408,800	1,616,788,037[16]	50.15%
Mr. Tian Diyong	Long	550,000	1,016,400	1,337,727,837	–	277,493,800	1,616,788,037[17]	50.15%
Mr. Shen Dingjian	Long	262,000	798,000	1,337,727,837	–	278,000,200	1,616,788,037[18]	50.15%
Benefit Way International Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[19]	50.15%
Mr. Liu Xuetian (deceased)	Long	–	–	–	1,348,180,237	268,607,800	1,616,788,037[20]	50.15%
Dobson Global Inc.	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[20]	50.15%
Ms. Qu Yihong	Long	–	–	1,348,180,237	–	268,607,800	1,616,788,037[21]	50.15%
Ms. Liu Ying	Long	–	–	1,348,180,237	–	268,607,800	1,616,788,037[21]	50.15%
Mr. Zhou Bing	Long	1,445,000	5,689,600	–	1,337,727,837	271,925,600	1,616,788,037[22]	50.15%
Darius Enterprises Limited	Long	–	–	1,337,727,837	–	279,060,200	1,616,788,037[22]	50.15%
Ms. Lv Lan	Long	519,000	1,906,800	1,337,727,837	–	276,634,400	1,616,788,037[23]	50.15%
Mr. Tian Yu	Long	515,000	1,148,000	1,337,727,837	–	277,397,200	1,616,788,037[24]	50.15%
Mr. Li Hanqiang	Long	345,000	1,027,600	1,337,727,837	–	277,687,600	1,616,788,037[25]	50.15%
Mr. Liu Yingguo	Long	242,000	448,000	1,337,727,837	–	278,370,200	1,616,788,037[26]	50.15%
Ms. Liu Lulu	Long	243,000	358,400	1,337,727,837	–	278,458,800	1,616,788,037[27]	50.15%
China Ocean Oilfields Services (Hong Kong) Limited	Long	–	174,425,609	–	–	–	174,425,609[28]	5.41%

Name	Long/Short position	Number of shares held: Personal interest: Share option	Personal interest: Shares interest	Corporate interest	Corporate interest and settlor of a discretionary trust	Interest of the Concert Group	Total	% of the issued share capital of the Company
China National Offshore Oil Corporation	Long	–	–	174,425,609	–	–	174,425,609(28)	5.41%
Nabors Drilling International II Limited	Long	–	450,000,000	–	–	–	450,000,000(29)	13.96%
Nabors International Management Limited	Long	–	–	450,000,000	–	–	450,000,000(29)	13.96%
Nabors Global Holdings Limited	Long	–	–	450,000,000	–	–	450,000,000(29)	13.96%
Nabors Industries Ltd.	Long	–	–	450,000,000	–	–	450,000,000(29)	13.96%
Carlyle Offshore Partners II. Ltd.	Long	–	–	166,841,887	–	–	166,841,887(30)	5.18%
DBD Cayman, Ltd	Long	–	–	166,841,887	–	–	166,841,887(30)	5.18%
TCG Holdings Cayman II, L.P.	Long	–	–	166,841,887	–	–	166,841,887(30)	5.18%

(1) Ally Giant Limited is wholly-owned by Ample Chance International Limited and holds 1,337,727,837 Shares.

(2) Ample Chance International Limited is owned approximately 36% by Ally Smooth Investments Limited, approximately 19.09% by Charm Moral International Limited, approximately 18.51% by Beauty Clear Holdings Limited, approximately 12.71% by Believe Power International Limited, approximately 10.50% by Benefit Way International Limited and approximately 3.19% by a corporation.

(3) The entire issued share capital of Ally Smooth Investments Limited is owned by Wealth Afflux Limited, which in turn is held by Equity Trustee Limited as trustee of The ZYL Family Trust. The ZYL Family Trust is a discretionary trust established by Zhang Mi as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The ZYL Family Trust are Zhang Mi and his family members. Zhang Mi is a member of the Concert Group.

(4) Charm Moral International Limited is owned approximately 41.34% by Mowbray Worldwide Limited, approximately 29.33% by Ecotech Enterprises Corporation and approximately 29.33% by Zheng Yong.

(5) Approximately 41.34% of the issued share capital of Charm Moral International Limited is owned by Mowbray Worldwide Limited, which in turn is held by Equity Trustee Limited as trustee of The RJDJ Victory Trust. The RJDJ Victory Trust is a discretionary trust established by Ren Jie as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The RJDJ Victory Trust are Ren Jie and his family members. Ren Jie is a member of the Concert Group.

(6) Approximately 29.33% of the issued share capital of Charm Moral International Limited is held by Ecotech Enterprises Corporation, which in turn is held by Equity Trustee Limited as trustee of The LZWM Family Trust. The LZWM Family Trust is a discretionary trust, established by Liu Zhi as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The LZWM Family Trust are Liu Zhi and his family members. Liu Zhi is a member of the Concert Group.

(7) Zheng Yong is the beneficial owner of approximately 29.33% of the issued share capital of Charm Moral International Limited, which is in turn the beneficial owner of 19.09% of the issued share capital of Ample Chance International Limited. Zheng Yong is a member of the Concert Group.

(8) Beauty Clear Holdings Limited is owned approximately 23.63% by Vast & Fast Corporation, approximately 22.77% by Cavendish Global Corporation, approximately 5.76% by Elegant Scene International Limited, approximately 5.10% by Chen Jun, and a total of approximately 42.74% by 3 other shareholders.

(9) Approximately 23.63% of the issued share capital of Beauty Clear Holdings Limited is owned by Vast & Fast Corporation, which in turn is held by Equity Trustee Limited as trustee of The ZHH Family Trust. The ZHH Family Trust is a discretionary trust, established by Zuo Huixian as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The ZHH Family Trust are Zuo Huixian and his family members. Zuo Huixian is a member of the Concert Group.

(10) Approximately 22.77% of the issued share capital of Beauty Clear Holdings Limited is held by Cavendish Global Corporation, which in turn is held by Equity Trustee Limited as trustee of The Hong Xu Family Trust. The Hong Xu Family Trust is a discretionary trust, established by Zhang Xu as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The Hong Xu Family Trust are Zhang Xu and his family members. Zhang Xu is a member of the Concert Group.

(11) Approximately 5.76% of the issued share capital of Beauty Clear Holdings Limited is held by Elegant Scene International Limited, which in turn wholly-owned by Wang Jiangyang. Beauty Clear Holdings Limited is the beneficial owner of approximately 18.51% of the issued share capital of Ample Chance International Limited. Wang Jiangyang is a member of the Concert Group.

(12) Chen Jun is the beneficial owner of approximately 5.10% of the issued share capital of Beauty Clear Holdings Limited, which in turn is the beneficial owner of approximately 18.51% of the issued share capital of Ample Chance International Limited. Chen Jun is a member of the Concert Group.

(13) Believe Power International Limited is owned approximately 32.72% by Brondesbury Enterprises Limited, approximately 29.16% by Zhang Yanyong, approximately 5.53% by Ao Pei, approximately 2.85% by Tian Diyong, approximately 2.24% by Shen Dingjian, and a total of approximately 27.50% by 4 other shareholders.

(14) Approximately 32.72% of the issued share capital of Believe Power International Limited is held by Brondesbury Enterprises Limited, which in turn is held by Equity Trustee Limited as trustee of The FBX Family Trust. The FBX Family Trust is a discretionary trust, established by Fan Bing as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The FBX Family Trust are Fan Bing and his family members. Fan Bing is a member of the Concert Group.

(15) Zhang Yanyong is the beneficial owner of approximately 29.16% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Zhang Yanyong is a member of the Concert Group.

(16) Ao Pei is the beneficial owner of approximately 5.53% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Ao Pei is a member of the Concert Group.

(17) Tian Diyong is the beneficial owner of approximately 2.85% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Tian Diyong is a member of the Concert Group.

(18) Shen Dingjian is the beneficial owner of approximately 2.24% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Shen Dingjian is a member of the Concert Group.

(19) Benefit Way International Limited is owned approximately 35.57% by Dobson Global Inc., approximately 19.36% by Darius Enterprises Limited, approximately 6.49% by Lv Lan, approximately 3.91% by Tian Yu, approximately 3.50% by Li Hanqiang, approximately 1.52% by Liu Yingguo, approximately 1.22% by Liu Lulu and approximately 28.43% by 6 other shareholders.

(20) Approximately 35.57% of the issued share capital of Benefit Way International Limited is held by Dobson Global Inc., which in turn is held by Equity Trustee Limited as trustee of The LXYY Family Trust. The LXYY Family Trust is a discretionary trust, established by Liu Xuetian (deceased) as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The LXYY Family Trust are Liu Xuetian (deceased) and his family members. Liu Xuetian (deceased) was a member of the Concert Group and passed away on 23 January 2008.

(21) Qu Yihong and Liu Ying, family members of Liu Xuetian (deceased), are deemed to be interested in 1,348,180,237 Shares as directors of Dobson Global Inc.

(22) Approximately 19.36% of the issued share capital of Benefit Way International Limited is held by Darius Enterprises Limited, which in turn is held by Equity Trustee Limited as trustee of The Fang Zhou Family Trust. The Fang Zhou Family Trust is a discretionary trust, established by Zhou Bing as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The Fang Zhou Family Trust are Zhou Bing and his family members. Zhou Bing is a member of the Concert Group.

(23) Lv Lan is the beneficial owner of approximately 6.49% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of the issued share capital of Ample Chance International Limited. Lu Lan is a member of the Concert Group.

(24) Tian Yu is the beneficial owner of approximately 3.91% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of the issued share capital of Ample Chance International Limited. Tian Yu is a member of the Concert Group.

(25) Li Hanqiang is the beneficial owner of approximately 3.50% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of the issued share capital of Ample Chance International Limited. Li Hanqiang is a member of the Concert Group.

(26) Liu Yingguo is the beneficial owner of approximately 1.52% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of the issued share capital of Ample Chance International Limited. Liu Yingguo is a member of the Concert Group.

(27) Liu Lulu is the beneficial owner of approximately 1.22% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of the issued share capital of Ample Chance International Limited. Liu Lulu is a member of the Concert Group.

(28) China Ocean Oilfields Services (Hong Kong) Limited holds 174,425,609 Shares. The issued share capital of China Ocean Oilfields Services (Hong Kong) Limited was beneficially owned approximately 99.35% by China National Offshore Oil Corporation and approximately 0.65% by Overseas Oil & Gas Corporation Limited.

(29) Nabors Drilling International II Limited ("NDIL II") holds 450,000,000 shares. NDIL II is a direct, wholly owned subsidiary of Nabors International Management Limited ("NIML"). NIML is a direct, wholly owned subsidiary of Nabors Global Holdings Limited which is in turn wholly owned by Nabors Industries Ltd.

(30) Carlyle Offshore Partners II. Ltd. owns 100% of DBD Cayman Ltd., which in turn owns 100% of TCG Holdings Cayman II, L.P., which in turn is holding subsidiaries that hold 166,841,887 shares.

Save as disclosed above, to the best of the Directors and the Chief Executives of the Company's knowledge, as at 30 June 2010, none of the persons, other than the Directors or the Chief Executives of the Company, had interests or short positions in the Shares and underlying Shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO or recorded in the register as required under Section 336 of the SFO.

SHARE OPTION SCHEME

(A) Pre-IPO Share Option Scheme

The principal terms of Pre-IPO share option scheme have been approved by resolutions in writing by all the Shareholders on 21 January 2008. As at the date of this report, a total of 270 eligible participants have been conditionally granted share options to subscribe for an aggregate of 60,000,000 Shares at an exercise price of offer price of HK$3.83 per Share. As at 30 June 2010, none of the grantees has exercised the share options granted to him/her under the Pre-IPO share option scheme and 717,000 shares options have been lapsed.

Each share option granted under the Pre-IPO share option scheme is exercisable within a period of five years commencing from 7 March 2008 (the "Listing Date") and the vesting period is ten years from the dated of grant. As at 30 June, 2010, 60% of the total number of the share options granted (if not cancelled) or 36,000,000 share options can be exercised under the Pre-IPO share option scheme.

No further options were granted under Pre-IPO share option scheme on or after the Listing Date.

(B) Share Option Scheme after Listing

On 15 April 2009, options to subscribe for 60,000,000 Shares of HK$0.10 each were granted to the eligible participants at an exercise price of HK$1.27 per Share under the Share Option Scheme adopted by resolutions in writing of all the Shareholders on 21 January 2008.

Under the Share Option Scheme, the share options are exercisable on or after 1 December 2009 by the grantees in the following manners: (1) up to 30% of the share options granted to each grantee from 1 December 2009 to 14 April 2010; (2) up to 60% of the share options granted to each grantee on or before 14 April 2011; (3) all the remaining share options granted to each grantee on or after 15 April 2011, and in each case, not later than 14 April 2019.

The valid period of the Share Option Scheme is up to 14 April 2019. Particulars and movements of share options under the Share Option Scheme during the six months ended 30 June 2010 were as follows:

	Number of share options									
Name or category of participant	Outstanding as at 1 January 2010	Granted during the six months ended 30 June 2010	Exercised during the six months ended 30 June 2010	Lapsed during the six months ended 30 June 2010	Cancelled during the six months ended 30 June 2010	Outstanding as at 30 June 2010	Date of grant (DD/MM/YY)	Exercise period (DD/MM/YY)	Exercise price per Share HK$	Price per Share immediately preceding the grant date of share options HK$
Directors										
Mr. Zhang Mi	3,937,000	–	–	–	–	3,937,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Liu Zhi	2,373,000	–	–	–	–	2,373,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Ren Jie	2,587,000	–	–	–	–	2,587,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Chen Guoming	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Liu Xiaofeng	1,000,000	–	–	–	–	1,000,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Liu Yinchun (Resigned as an Independent Non-Executive Director with effect on 14/04/2010)	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Qi Daqing	1,000,000	–	–	–	–	1,000,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Tai Kwok Leung, Alexander	850,000	–	–	–	–	850,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Wang Li	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Shi Xingquan	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Sub-total	14,747,000	–	–	–	–	14,747,000				

Name or category of participant	Number of share options: Outstanding as at 1 January 2010	Granted during the six months ended 30 June 2010	Exercised during the six months ended 30 June 2010	Lapsed during the six months ended 30 June 2010	Cancelled during the six months ended 30 June 2010	Outstanding as at 30 June 2010	Date of grant (DD/MM/YY)	Exercise period (DD/MM/YY)	Exercise price per Share HK$	Price per Share immediately preceding the grant date of share options HK$
Substantial Shareholders										
Mr. Zheng Yong	695,000	–	–	–	–	695,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Zuo Huixian	674,000	–	–	–	–	674,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Zhang Xu	642,000	–	–	–	–	642,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Wang Jiangyang	301,000	–	–	–	–	301,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Chen Jun	332,000	–	–	–	–	332,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Fan Bing	569,000	–	–	–	–	569,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Zhang Yanyong	480,000	–	–	–	–	480,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Ao Pei	243,000	–	–	–	–	243,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Tian Diyong	195,000	–	–	–	–	195,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Shen Dingjian	87,000	–	–	–	–	87,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Zhou Bing	695,000	–	–	–	–	695,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Ms. Lv Lan	174,000	–	–	–	–	174,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Tian Yu	275,000	–	–	–	–	275,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Li Hanqiang	130,000	–	–	–	–	130,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Liu Yingguo	117,000	–	–	–	–	117,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Ms. Liu Lulu	108,000	–	–	–	–	108,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Sub–total	5,717,000	–	–	–	–	5,717,000				
Other										
Employee	38,827,300	–	579,300	190,700	–	38,057,300	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Sub–total	38,827,300	–	579,300	190,700	–	38,057,300				
Total	59,291,300	–	579,300	190,700	–	58,521,300				

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's Shares during the six months ended 30 June 2010.

AUDIT COMMITTEE

The Audit Committee comprises all the Independent Non-executive Directors with written terms of reference in compliance with the Listing Rules. The Audit Committee is responsible for reviewing and supervising financial reporting process and internal control systems and providing advices and recommendations to the Board. The Audit Committee shall hold at least two meetings a year and review opinions of internal auditors, matters in respects of internal control, risk management and financial reporting. The Audit Committee has reviewed the interim results of the Group for the six months ended 30 June 2010.

COMPLIANCE WITH THE CODE ON CORPORATE GOVERANCE PRACTICES

The Company has complied with the principles as set out in the CG Code throughout the six months ended 30 June 2010, except the following deviations:

Based on the Rule A.2.1 of CG Code, the positions of Chairman and President (Chief Executive Officer) should be separated and should not be performed by the same individual. However, Mr. Zhang Mi is the Chairman of the Board and President (Chief Executive Officer) of the Company. Mr. Zhang Mi is the main founder of the Group and has extensive experience in the industry and related industries. In the opinion of the Board, the vesting of duties of Chairman of the Board and President (Chief Executive Officer) of the Company to Mr. Zhang Mi would provide a strong and consistent leadership and allow effective planning and executing business decisions and strategies, as well as ensure the interests of the shareholders as a whole. On the other hand, the balance between powers and duties could be ensured through the operation of the Board and the committees under it. The Company will continue to review the effectiveness of the Group's corporate governance structure and consider whether it needs to make any changes, including the separation of duties and Chairman of the Board and President (Chief Executive Officer) of the Company.

On behalf of the Board of
Honghua Group Limited
Zhang Mi
Chairman

Hong Kong, 30 August 2010

Independent Review Report

To the board of directors of Honghua Group Limited
(Incorporated in the Cayman Islands with limited liability)

INTRODUCTION

We have reviewed the interim financial report set out on pages 31 to 63 which comprises the consolidated balance sheet of Honghua Group Limited as at 30 June 2010 and the related consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the condensed consolidated cash flow statement for the six months then ended and explanatory notes. The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of an interim financial report to be in compliance with the relevant provisions thereof and International Accounting Standard ("IAS") 34, *Interim financial reporting* adopted by the International Accounting Standards Board. The directors are responsible for the preparation and presentation of the interim financial report in accordance with IAS 34.

Our responsibility is to form a conclusion, based on our review, on the interim financial report and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

SCOPE OF REVIEW

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410, *Review of interim financial information performed by the independent auditor of the entity*, issued by the Hong Kong Institute of Certified Public Accountants. A review of the interim financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

CONCLUSION

Based on our review, nothing has come to our attention that causes us to believe that the interim financial report as at 30 June 2010 is not prepared, in all material respects, in accordance with IAS 34, *Interim financial reporting*.

KPMG
Certified Public Accountants
8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong

30 August 2010

Consolidated Income Statement

For the six months ended 30 June 2010 — unaudited
(Expressed in Renminbi)

	Note	Six months ended 30 June 2010 RMB'000	2009 RMB'000 (restated)
Revenue	3, 4	**685,596**	1,196,503
Cost of sales		**(523,929)**	(875,561)
Gross profit		**161,667**	320,942
Other operating revenue	5	**3,193**	2,991
Other operating expenses		**(1,227)**	(2,523)
Selling expenses		**(69,984)**	(111,849)
General and administrative expenses		**(148,997)**	(128,157)
Other net income	5	**1,253**	4,363
(Loss)/profit from operations		**(54,095)**	85,767
Finance income		**8,755**	44,055
Finance expenses		**(54,526)**	(41,218)
Net finance (expenses)/income	6(a)	**(45,771)**	2,837
Share of loss from jointly controlled entities		**(1,484)**	(2,152)
(Loss)/profit before taxation	6	**(101,350)**	86,452
Income tax credit/(expenses)	7	**12,176**	(20,333)
(Loss)/profit for the period		**(89,174)**	66,119
Attributable to:			
Equity shareholders of the Company		**(89,458)**	57,589
Non-controlling interests		**284**	8,530
(Loss)/profit for the period		**(89,174)**	66,119
(Loss)/earnings per share — Basic and diluted (RMB cents)	8		
Basic		**(2.77)**	1.79
Diluted		**(2.77)**	1.79

The accompanying notes form part of this interim financial report.

Consolidated Statement of Comprehensive Income

For the six months ended 30 June 2010 — unaudited
(Expressed in Renminbi)

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
		(restated)
(Loss)/profit for the period	**(89,174)**	66,119
Other comprehensive income for the period:		
Exchange differences on translation of financial statements of operations outside the People's Republic of China ("PRC")	**(18,504)**	(715)
Total comprehensive income for the period	**(107,678)**	65,404
Attributable to:		
Equity shareholders of the Company	**(107,969)**	56,874
Non-controlling interests	**291**	8,530
Total comprehensive income for the period	**(107,678)**	65,404

The accompanying notes form part of this interim financial report.

Consolidated Balance Sheet

At 30 June 2010 — unaudited
(Expressed in Renminbi)

	Note	30 June 2010 RMB'000	31 December 2009 RMB'000 (restated)
Non-current assets			
Fixed assets			
— Property, plant and equipment		**419,457**	414,746
— Interests in leasehold land held for own use under operating leases		**140,943**	141,829
— Freehold land		**5,474**	5,504
	9	**565,874**	562,079
Deposit paid for acquisition of leasehold land		**213,844**	209,308
Construction in progress		**105,147**	59,144
Intangible assets	10	**297,699**	318,859
Interests in jointly controlled entities		**8,573**	10,309
Deferred tax assets		**61,502**	49,372
Total non-current assets		**1,252,639**	1,209,071
Current assets			
Inventories	11	**1,856,074**	1,896,646
Trade and other receivables	12	**1,021,285**	1,246,351
Amounts due from related companies		**26,842**	31,096
Amount due from immediate holding company		**12**	6
Amount due from ultimate holding company		**—**	6
Current tax recoverable		**24,103**	24,393
Other financial assets	13	**3,700**	—
Pledged bank deposits	14	**47,757**	30,663
Bank deposits maturing over three months		**130,000**	542,898
Cash and cash equivalents		**1,541,415**	1,603,316
Total current assets		**4,651,188**	5,375,375
Total assets		**5,903,827**	6,584,446
Current liabilities			
Interest-bearing borrowings	15	**805,466**	1,046,090
Amounts due to related companies		**4,041**	5,609
Trade and other payables	16	**792,639**	974,024
Current tax payable		**14,284**	20,933
Provision for product warranties		**12,927**	15,579
Total current liabilities		**1,629,357**	2,062,235

Consolidated Balance Sheet

At 30 June 2010 — unaudited
(Expressed in Renminbi)

	Note	30 June 2010 RMB'000	31 December 2009 RMB'000 (restated)
Net current assets		**3,021,831**	3,313,140
Total assets less current liabilities		**4,274,470**	4,522,211
Non-current liabilities			
Interest-bearing borrowings	15	**102,377**	252,390
Deferred tax liabilities		**9,225**	10,414
Total non-current liabilities		**111,602**	262,804
Total liabilities		**1,740,959**	2,325,039
Equity			
Share capital	17(a)	**299,593**	299,542
Reserves	17(b)	**3,767,951**	3,864,841
Total equity attributable to equity shareholders of the Company		**4,067,544**	4,164,383
Non-controlling interests		**95,324**	95,024
Total equity		**4,162,868**	4,259,407
Total liabilities and equity		**5,903,827**	6,584,446

Approved and authorised for issue by the board of directors on 30 August 2010.

Zhang Mi
Director

Liu Zhi
Director

The accompanying notes form part of this interim financial report.

Consolidated Statement of Changes in Equity

For the six months ended 30 June 2010 — unaudited
(Expressed in Renminbi)

		Attributable to equity shareholders of the Company									
	Note	Share capital (Note 17(a)) RMB'000	Share premium (Note 17(b) (v)) RMB'000	Other reserve (Note 17(b) (iii)) RMB'000	Capital reserve (Note 17(b) (iv)) RMB'000	Surplus reserve (Note 17(b) (i)) RMB'000	Exchange reserve (Note 17(b) (ii)) RMB'000	Retained profits RMB'000	Subtotal RMB'000	Non-controlling interests RMB'000	Total equity RMB'000
At 1 January 2010, as previously reported		**299,542**	**2,476,705**	**57,510**	**471,185**	**211,551**	**(77,742)**	**730,154**	**4,168,905**	**95,024**	**4,263,929**
Prior period adjustment in respect of change in accounting policy		**–**	**–**	**–**	**–**	**–**	**–**	**(4,522)**	**(4,522)**	**–**	**(4,522)**
At 1 January 2010 (restated)		**299,542**	**2,476,705**	**57,510**	**471,185**	**211,551**	**(77,742)**	**725,632**	**4,164,383**	**95,024**	**4,259,407**
Capital injection by non-controlling interests		**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**9**	**9**
Equity-settled share-based transactions		**–**	**–**	**–**	**10,482**	**–**	**–**	**–**	**10,482**	**–**	**10,482**
Shares issued under share option scheme		**51**	**814**	**–**	**(217)**	**–**	**–**	**–**	**648**	**–**	**648**
Options lapsed under share option schemes		**–**	**–**	**–**	**(15)**	**–**	**–**	**15**	**–**	**–**	**–**
Total comprehensive income for the period		**–**	**–**	**–**	**–**	**–**	**(18,511)**	**(89,458)**	**(107,969)**	**291**	**(107,678)**
At 30 June 2010		**299,593**	**2,477,519**	**57,510**	**481,435**	**211,551**	**(96,253)**	**636,189**	**4,067,544**	**95,324**	**4,162,868**
At 1 January 2009, as previously reported		299,495	2,508,202	59,358	436,796	199,490	(76,424)	1,007,465	4,434,382	93,026	4,527,408
Prior period adjustment in respect of change in accounting policy		–	–	–	–	–	–	(3,896)	(3,896)	–	(3,896)
At 1 January 2009 (restated)		299,495	2,508,202	59,358	436,796	199,490	(76,424)	1,003,569	4,430,486	93,026	4,523,512
Dividends approved in respect of the previous financial year	17(c)	–	–	–	–	–	–	(170,371)	(170,371)	–	(170,371)
Dividends to non-controlling interests		–	–	–	–	–	–	–	–	(5,104)	(5,104)
Equity-settled share-based transactions		–	–	–	15,385	–	–	–	15,385	–	15,385
Total comprehensive income for the period		–	–	–	–	–	(715)	57,589	56,874	8,530	65,404
At 30 June 2009		299,495	2,508,202	59,358	452,181	199,490	(77,139)	890,787	4,332,374	96,452	4,428,826

The accompanying notes form part of this interim financial report.

Condensed Consolidated Cash Flow Statement

For the six months ended 30 June 2010 — unaudited
(Expressed in Renminbi)

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
Cash generated from operations	**16,128**	132,833
Tax paid	**(7,427)**	(67,615)
Net cash generated from operating activities	**8,701**	65,218
Net cash generated from investing activities	**345,770**	99,470
Net cash used in financing activities	**(412,317)**	(421,818)
Net decrease in cash and cash equivalents	**(57,846)**	(257,130)
Cash and cash equivalents at 1 January	**1,603,316**	1,467,363
Effect of foreign exchange rate changes	**(4,055)**	—
Cash and cash equivalents at 30 June	**1,541,415**	1,210,233

The accompanying notes form part of this interim financial report.

Notes to the Condensed Consolidated Interim Financial Report

(Expressed in Renminbi)

1 BASIS OF PRESENTATION AND PREPARATION

(a) General information

Honghua Group Limited (the "Company") was incorporated in the Cayman Islands on 15 June 2007 as an exempted company with limited liability under the Companies Law, Cap 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands.

The interim financial report for the six months ended 30 June 2010 comprises the Company and its subsidiaries (collectively referred to as the "Group") and the Group's interests in jointly controlled entities.

During the six months ended 30 June 2010, the Group has established three entities, namely Honghua (China) Investment Co., Ltd, Hi Tech Drilling Company Limited and Sichuan Honghua International (H.K.) Limited, while Sichuan Honglian Industrial Co., Limited was liquidated. The change in composition of the Group does not have a material effect on the results of operation and financial position of the Group for the interim period presented.

(b) Basis of preparation

The interim financial report has been prepared in accordance with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standard ("IAS") 34, *Interim financial reporting*, adopted by the International Accounting Standards Board ("IASB"). It was authorised for issuance on 30 August 2010.

The interim financial report has also been prepared in accordance with the same accounting policies adopted by the Group in the 2009 annual financial statements, except for the accounting policy changes that are expected to be reflected in the 2010 annual financial statements. Details of these changes in accounting policies are set out in note 2.

The preparation of an interim financial report in conformity with IAS 34 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses on a year to date basis. Actual results may differ from these estimates.

In preparing this interim financial report, the significant judgements made by management in applying the Group's accounting policies and key sources of estimation uncertainty were the same as those that applied to the 2009 annual financial statements.

1 BASIS OF PRESENTATION AND PREPARATION (continued)

(b) Basis of preparation (continued)

This interim financial report contains condensed consolidated financial statements and selected explanatory notes. The notes include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Group since the 2009 annual financial statements. The condensed consolidated interim financial statements and notes thereon do not include all of the information required for a full set of financial statements prepared in accordance with International Financial Reporting Standards ("IFRSs").

The interim financial report is unaudited, but has been reviewed by KPMG in accordance with Hong Kong Standard on Review Engagements 2410, *Review of interim financial information performed by the independent auditor of the entity*, issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). KPMG's independent review report to the Board of Directors is included on page 30.

The interim financial report is presented in Renminbi ("RMB"), rounded to the nearest thousand, on the historical cost basis.

The financial information relating to the financial year ended 31 December 2009 that is included in the interim financial report as being previously reported information does not constitute the Company's statutory financial statements for that financial year but is derived from those financial statements. Statutory financial statements for the year ended 31 December 2009 are available from the Company's registered office. The auditors have expressed an unqualified opinion on those financial statements in their report dated 13 April 2010.

2 CHANGES IN ACCOUNTING POLICIES

(a) New accounting policies

The IASB has issued two revised IFRSs, a number of amendments to IFRSs and one new Interpretation that are first effective for the current accounting period of the Group and the Company. Of these, the following developments are relevant to the Group's financial statements:

— IFRS 3 (revised 2008), *Business combinations*

— Amendments to IAS 27, *Consolidated and separate financial statements*

— Improvements to IFRSs (2009)

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period.

2 CHANGES IN ACCOUNTING POLICIES (continued)

(a) New accounting policies (continued)

The developments resulted in changes in accounting policy but none of these changes in policy have a material impact on the current or comparative periods, for the following reasons:

— The impact of the majority of the revisions to IFRS 3 and IAS 27 have not yet had a material effect on the Group's financial statements as these changes will first be effective as and when the Group enters into a relevant transaction (for example, a business combination, a disposal of a subsidiary or a non-cash distribution) and there is no requirement to restate the amounts recorded in respect of previous such transactions.

— The impact of the amendments to IFRS 3 (in respect of recognition of acquiree's deferred tax assets) and IAS 27 (in respect of allocation of losses to non-controlling interests (previously known as minority interests) in excess of their equity interest) have had no material impact as there is no requirement to restate amounts recorded in previous periods and no such deferred tax assets or losses arose in the current period.

Further details of these changes in accounting policy are as follows:

— As a result of the adoption of IFRS 3 (revised 2008), any business combination acquired on or after 1 January 2010 will be recognised in accordance with the new requirements and detailed guidance contained in IFRS 3 (revised 2008). These include the following changes in accounting policies:

  — Transaction costs that the Group incurs in connection with a business combination, such as finder's fees, legal fees, due diligence fees, and other professional and consulting fees, will be expensed as incurred, whereas previously they were accounted for as part of the cost of the business combination and therefore impacted the amount of goodwill recognised.

  — If the Group holds interests in the acquiree immediately prior to obtaining control, these interests will be treated as if disposed of and re-acquired at fair value on the date of obtaining control. Previously, the step-up approach would have been applied, whereby goodwill was computed as if accumulated at each stage of the acquisition.

2 CHANGES IN ACCOUNTING POLICIES (continued)

(a) New accounting policies (continued)

— Contingent consideration will be measured at fair value at the acquisition date. Any subsequent changes in the measurement of that contingent consideration will be recognised in profit or loss, unless they arise from obtaining additional information about facts and circumstances that existed at the acquisition date within 12 months from the date of acquisition (in which case they will be recognised as an adjustment to the cost of the business combination). Previously, contingent consideration was recognised at the acquisition date only if payment of the contingent consideration was probable and it could be measured reliably. All subsequent changes in the measurement of contingent consideration and from its settlement were previously recognised as an adjustment to the cost of the business combination and therefore impacted the amount of goodwill recognised.

— If the acquiree has accumulated tax losses or other temporary deductible differences and these fail to meet the recognition criteria for deferred tax assets at the date of acquisition, then any subsequent recognition of these assets will be recognised in profit or loss, rather than as an adjustment to goodwill as was previously the policy.

— In addition to the Group's existing policy of measuring the non-controlling interests (previously known as the "minority interests") in the acquiree at the non-controlling interest's proportionate share of the acquiree's net identifiable assets, in future the group may elect, on a transaction by transaction basis, to measure the non-controlling interest at fair value.

In accordance with the transitional provisions in IFRS 3 (revised 2008), these new accounting policies will be applied prospectively to any business combinations in the current or future periods. The new policy in respect of recognition in the movement of deferred tax assets will also be applied prospectively to accumulated tax losses and other temporary deductible differences acquired in previous business combinations. No adjustments have been made to the carrying values of assets and liabilities that arose from business combinations whose acquisition dates preceded the application of this revised standard.

— As a result of the adoption of IAS 27 (amended 2008), the following changes in policies will be applied as from 1 January 2010:

2 CHANGES IN ACCOUNTING POLICIES (continued)

(a) New accounting policies (continued)

- If the Group acquires an additional interest in a non-wholly owned subsidiary, the transaction will be accounted for as a transaction with equity shareholders (the non-controlling interests) in their capacity as owners and therefore no goodwill will be recognised as a result of such transactions. Similarly, if the Group disposes of part of its interest in a subsidiary but still retains control, this transaction will also be accounted for as a transaction with equity shareholders (the non-controlling interests) in their capacity as owners and therefore no profit or loss will be recognised as a result of such transactions.

- If the Group loses control of a subsidiary, the transaction will be accounted for as a disposal of the entire interest in that subsidiary, with any remaining interest retained by the Group being recognised at fair value as if reacquired. In addition, as a result of the adoption of the amendment to IFRS 5, if at the balance sheet date the Group has the intention to dispose of a controlling interest in a subsidiary, the entire interest in that subsidiary will be classified as held for sale (assuming that the held for sale criteria in IFRS 5 are met) irrespective of the extent to which the Group will retain an interest. Previously such transactions were treated as partial disposals.

In accordance with the transitional provisions in IAS 27, these new accounting policies will be applied prospectively to transactions in current or future periods and therefore previous periods have not been restated.

- In order to be consistent with the above amendments to IFRS 3 and IAS 27, and as a result of amendments to IAS 28, *Investments in associates*, and IAS 31, *Interests in joint ventures*, the following policies will be applied as from 1 January 2010.

  - If the Group holds interests in the acquiree immediately prior to obtaining significant influence or joint control, these interests will be treated as if disposed of and re-acquired at fair value on the date of obtaining significant influence or joint control. Previously, the step-up approach would have been applied, whereby goodwill was computed as if accumulated at each stage of the acquisition.

  - If the Group loses significant influence or joint control, the transaction will be accounted for as a disposal of the entire interest in that investee, with any remaining interest being recognised at fair value as if reacquired. Previously such transactions were treated as partial disposals.

  Consistent with the transitional provisions in IFRS 3 and IAS 27, these new accounting policies will be applied prospectively to transactions in current or future periods and therefore previous periods have not been restated.

2 CHANGES IN ACCOUNTING POLICIES (continued)

(a) New accounting policies (continued)

Other changes in accounting policies which are relevant to the Group's financial statements are as follows:

— As a result of the amendments to IAS 27, as from 1 January 2010 any losses incurred by a non-wholly owned subsidiary will be allocated between the controlling and non-controlling interests in proportion to their interests in that entity, even if this results in a deficit balance within consolidated equity being attributed to the non-controlling interests. Previously, if the allocation of losses to the non-controlling interests would have resulted in a deficit balance, the losses were only allocated to the non-controlling interests if the non-controlling interests were under a binding obligation to make good the losses. In accordance with the transitional provisions in IAS 27, this new accounting policy is being applied prospectively and therefore previous periods have not been restated.

— As a result of the amendment to IAS 17, *Leases*, arising from the "*Improvements to IFRSs (2009)*" omnibus standard, the Group has re-evaluated the classification of its interests in leasehold land as to whether, in the Group's judgement, the lease transfers significantly all the risks and rewards of ownership of the land such that the Group is in a position economically similar to that of a purchaser. The Group has concluded that the classification of such leases as operating leases continues to be appropriate.

(b) Change in application of accounting policies

In previous years, the Group's inventories were carried at the lower of cost and net realisable value. The cost was calculated using the first-in first-out formula. Following the substantial business development of the Group in recent years, the directors of the Company are of the view that it is no longer practicable for the Group to continue adopting such accounting policy whereas using the weighted-average formula would result in the consolidated financial statements providing more appropriate and relevant information about the Group's results and financial position to the users of the financial statements. Consequently, the Group changed its accounting policy on inventories to follow the weighted-average formula with effect from 1 January 2010.

2 CHANGES IN ACCOUNTING POLICIES (continued)

(b) Change in application of accounting policies (continued)

This change in accounting policy has been applied retrospectively with comparatives restated. The adjustments for each financial statement line item affected for the six months ended 30 June 2010 and 2009 are set out below:

Consolidated income statement for the six months ended 30 June

	2010 RMB'000	2009 RMB'000
Increase in net loss/(profit)		
Cost of sales	**1,159**	(1,476)
(Loss)/profit for the period	**1,159**	(1,476)
Attributable to:		
— Equity shareholders of the Company	**1,159**	(1,476)
— Non-controlling interests	**—**	—
(Loss)/earnings per share (basic) in cents	**0.04**	(0.05)
(Loss)/earnings per share (diluted) in cents	**0.04**	(0.05)

Consolidated statement of changes in equity for the six months ended 30 June

	2010 RMB'000	2009 RMB'000
(Decrease)/increase in total equity		
Total equity at 1 January	**(4,522)**	(3,896)
Total comprehensive income for the period	**(1,159)**	1,476
Total equity at 30 June	**(5,681)**	(2,420)

2 CHANGES IN ACCOUNTING POLICIES (continued)

(b) Change in application of accounting policies (continued)

Consolidated balance sheet

	30 June 2010 RMB'000	31 December 2009 RMB'000	1 January 2009 RMB'000
Decrease in net assets			
Inventories	**(5,681)**	(4,522)	(3,896)
Net current assets	**(5,681)**	(4,522)	(3,896)
Net assets	**(5,681)**	(4,522)	(3,896)
Retained profits and total equity	**(5,681)**	(4,522)	(3,896)

3 SEGMENT REPORTING

Information regarding the Group's reportable segments as provided to the Group's most senior executive management for the purposes of resource allocation and assessment of segment performance for the period is set out below.

For the six months ended 30 June	Drilling rigs 2010 RMB'000	Drilling rigs 2009 RMB'000 (restated)	Parts and components 2010 RMB'000	Parts and components 2009 RMB'000 (restated)	Total 2010 RMB'000	Total 2009 RMB'000 (restated)
Revenue from external customers	**466,642**	1,023,699	**218,954**	172,804	**685,596**	1,196,503
Inter-segment revenue	**—**	—	**139,423**	459,170	**139,423**	459,170
Reportable segment revenue	**466,642**	1,023,699	**358,377**	631,974	**825,019**	1,655,673
Reportable segment (loss)/profit	**(27,501)**	125,963	**20,859**	92,074	**(6,642)**	218,037

As at 30 June/ 31 December	Drilling rigs 2010 RMB'000	Drilling rigs 2009 RMB'000 (restated)	Parts and components 2010 RMB'000	Parts and components 2009 RMB'000 (restated)	Total 2010 RMB'000	Total 2009 RMB'000 (restated)
Reportable segment assets	**2,738,852**	2,914,246	**1,068,535**	1,303,947	**3,807,387**	4,218,193

3 SEGMENT REPORTING (continued)

(a) Reconciliation of reportable segment profit or loss

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
		(restated)
(Loss)/profit		
Reportable segment (loss)/profit	**(6,642)**	218,037
Elimination of inter-segment profits	**(35,179)**	(135,934)
Reportable segment (loss)/profit derived from Group's external customers	**(41,821)**	82,103
Share of loss from jointly controlled entities	**(1,484)**	(2,152)
Other operating revenue, expenses and net income	**3,219**	4,831
Net finance (expenses)/income	**(45,771)**	2,837
Unallocated head office and corporate expenses	**(15,493)**	(1,167)
(Loss)/profit before taxation	**(101,350)**	86,452

(b) Seasonality of operations

The Group experiences higher sales in the second half of the year compared to the first half of the year. It is the general practice for the Group's customers, engaging in oil and gas drilling industry, to place larger amounts of purchase orders at the beginning of the year. Having considered the production and delivery schedule, the finished goods related to these purchase orders are delivered in the second half of the year. Revenue from the sale of finished goods is recognised when the customer has accepted the related risks and rewards of ownership. Accordingly, the Group anticipates the inventories would gradually build up before the delivery of finished goods in the second half of the year. As a result, the first half year typically reports lower revenues and results, than the second half.

4 REVENUE

The principal activities of the Group are the manufacturing, sale and trading of drilling rigs and related parts and components. Revenue represents the sales value of goods supplied to customers less value-added tax, returns and trade discounts.

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
Sale of drilling rigs	**466,642**	1,023,699
Sale of parts and components	**218,954**	172,804
	685,596	1,196,503

For the six months ended 30 June 2010, the Group's customer base include three customers with whom transactions representing 29%, 24% and 22% (2009: 47%, 17% and 13%) of the Group's revenue respectively. In 2010, revenues from sales of drilling rigs and related parts and components to these customers, amounted to approximately RMB198 million, RMB166 million and RMB151 million (2009: RMB564 million, RMB200 million and RMB161 million) respectively which arose in North America, Europe and Central Asia, and South Asia regions.

5 OTHER OPERATING REVENUE AND OTHER NET INCOME

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
Other operating revenue		
Rendering of repairing services	**2,834**	2,523
Others	**359**	468
	3,193	2,991
Other net income		
Government grants	**3,666**	6,239
Loss on disposals of fixed assets	**(62)**	(726)
Realised gains on other financial assets	**1,201**	59
Donations	**(1,202)**	(220)
Others	**(2,350)**	(989)
	1,253	4,363

6 (LOSS)/PROFIT BEFORE TAXATION

(Loss)/profit before taxation is arrived at after charging/(crediting):

		Six months ended 30 June	
		2010	2009
		RMB'000	RMB'000
(a)	**Net finance expenses/(income)**		
	Exchange loss/(gain), net	**30,703**	(20,650)
	Interest income	**(8,755)**	(23,405)
	Interest on bank borrowings wholly repayable within five years	**26,712**	37,476
	Bank charges	**1,935**	3,742
		50,595	(2,837)
	Less: interest expense capitalised into assets under construction*	**(4,824)**	—
		45,771	(2,837)

* The borrowing costs have been capitalised at a rate of 0.68%–6.50% per annum (2009: Nil).

(b)	**Staff costs**		
	Contributions to defined contribution retirement scheme	**19,931**	13,098
	Equity-settled share based payment expenses	**10,482**	15,385
	Salaries, wages and other benefits	**106,098**	89,818
		136,511	118,301
(c)	**Other items**		
	Amortisation and depreciation		
	— assets held for use under operating leases	**886**	764
	— other assets	**23,736**	22,151
	— intangible assets	**18,350**	18,415
	Operating lease charges in respect of properties	**2,839**	2,263
	Provision for product warranties	**13,663**	5,875
	Research and development costs (note)	**18,888**	15,100

Note: The amounts included staff costs of employees in the Research and Development Department.

7 INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT

(a) Taxation in the consolidated income statement represents:

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
Current tax — outside Hong Kong		
Provision for the period	**2,234**	37,355
Over provision in respect of prior years	**(1,113)**	(3,614)
	1,121	33,741
Deferred tax		
Origination and reversal of temporary differences	**(13,297)**	(13,408)
	(12,176)	20,333

(i) Hong Kong

No provision for the Hong Kong Profits Tax has been made as the Group did not have assessable profits subject to Hong Kong Profits Tax for the period (2009: Nil).

(ii) PRC

Pursuant to the income tax rules and regulations of the PRC, the companies comprising the Group in the PRC are liable to PRC corporate income tax at a rate of 25% during the six months ended 30 June 2010 (2009: 25%), except for the following companies:

(a) Sichuan Honghua Petroleum Equipment Co., Ltd ("Honghua Company")

On 15 September 2006, Honghua Company changed from being a domestic enterprise to a wholly owned foreign invested enterprise, and was entitled to tax concessions from 1 October 2006 whereby the profit for the first two financial years commencing on the profit-making year (after netting off tax losses carried forward from prior years) was exempt from income tax in the PRC and the profit for each of the subsequent three financial years was taxed at 50% of the prevailing tax rate set by the relevant authorities. Therefore all income earned for the period from 1 January 2010 to 30 June 2010 are subject to an income tax rate of 12.5% (2009: 12.5%).

7 INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT (continued)

(a) Taxation in the consolidated income statement represents: (continued)

(ii) PRC (continued)

(b) Chengdu Hongtian Electric Drive Engineering Co., Ltd ("Hongtian Company") and Sichuan Honghua Youxin Petroleum Machinery Co., Ltd ("Youxin Company")

Hongtian Company and Youxin Company are recognised as entities established in the western regions of the PRC with principal revenue of over 70% generated from the encouraged business activities. Pursuant to the approvals obtained from the relevant PRC tax authorities, the companies are entitled to a preferential income tax rate of 15%.

(iii) Others

Taxation for other entities is charged at the appropriate current rates of taxation ruling in the relevant jurisdictions.

(b) Withholding tax

Under the PRC tax law and its Implementation Rules, dividends receivable by non-PRC resident enterprises from PRC resident enterprises are subject to withholding tax at a rate of 10% unless reduced by tax treaties or agreements. Under the *Arrangement between the Mainland of China and Hong Kong Special Administrative Region for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income*, Hong Kong tax residents which hold 25% or more of a PRC enterprise are entitled to a reduced dividend withholding tax rate of 5%. Pursuant to CaiShui 2008 No. 1 *Notice on Certain Preferential Enterprise Income Tax Policies*, undistributed earnings generated prior to 1 January 2008 are exemption from such withholding tax. Accordingly, dividends receivable by Honghua Holdings Limited ("Honghua Holdings") from its subsidiaries established in the PRC in respect of their profits earned since 1 January 2008 is subject to 5% withholding tax. Deferred tax liabilities have been recognised for undistributed retained profits of its subsidiaries established in the PRC earned since 1 January 2008 to the extent that profits are likely to be distributed in the foreseeable future.

8 (LOSS)/EARNINGS PER SHARE

(a) Basic (loss)/earnings per share

The calculation of basic (loss)/earnings per share for the six months ended 30 June 2010 is based on the loss attributable to shareholders of the Company for the period of RMB89,458,000 (six months ended 30 June 2009 (restated): a profit of RMB57,589,000) and the weighted average number of shares of 3,223,782,961 (2009: 3,223,688,000) in issue during the interim period.

(b) Diluted (loss)/earnings per share

The calculation of diluted (loss)/earnings per share is based on the loss attributable to shareholders of the Company for the period of RMB89,458,000 and the weighted average number of shares of 3,224,493,154 in issue during the interim period.

There were no dilutive potential ordinary shares for the six months ended 30 June 2009 and, therefore, dilutive earnings per share are the same as the basic earnings per share.

9 FIXED ASSETS

	2010 **RMB'000**	2009 RMB'000
Net book value, at 1 January	**562,079**	434,139
Additions	**24,700**	15,019
Transfer from construction in progress	**4,616**	15,965
Disposals (net carrying amount)	**(685)**	(836)
Amortisation and depreciation charge for the period	**(24,622)**	(22,915)
Exchange difference	**(214)**	(15)
Net book value, at 30 June	**565,874**	441,357

Included in fixed assets were interests in leasehold land held for own use under operating leases, which represent prepayments for land use rights in the PRC with a medium-term lease.

Notes to the Condensed Consolidated Interim Financial Report

(Expressed in Renminbi)

10 INTANGIBLE ASSETS

	2010	2009
	RMB'000	RMB'000
Net book value, at 1 January	**318,859**	356,216
Amortisation for the period	**(18,350)**	(18,415)
Exchange difference	**(2,810)**	(163)
Net book value, at 30 June	**297,699**	337,638

11 INVENTORIES

	30 June 2010	31 December 2009
	RMB'000	RMB'000 (restated)
Raw materials	**681,352**	826,213
Work in progress	**625,578**	536,948
Finished goods	**542,906**	529,288
Goods in transit	**6,238**	4,197
	1,856,074	1,896,646

An analysis of the amount of inventories recognised as an expense is as follows:

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000 (restated)
Carrying amount of inventories sold	**500,801**	843,874
Write-down of inventories	**9,702**	25,812
Reversal of write-down of inventories	**(237)**	—
	510,266	869,686

12 TRADE AND OTHER RECEIVABLES

	30 June 2010 RMB'000	31 December 2009 RMB'000
Trade receivables	**737,511**	901,707
Bills receivable	**3,000**	2,200
Less: allowance for doubtful debts (note 12(b))	**(125,345)**	(124,669)
Sub-total	**615,166**	779,238
Value-added tax receivable	**171,430**	191,450
Prepayments	**134,573**	154,884
Other receivables	**100,116**	120,779
	1,021,285	1,246,351

All of the trade and other receivables are expected to be recovered within one year.

(a) Ageing analysis

Included in trade and other receivables are trade receivables and bills receivable (net of allowance for doubtful debts) with the following ageing analysis as of the balance sheet date:

	30 June 2010 RMB'000	31 December 2009 RMB'000
Current	**183,469**	276,849
Less than 1 month past due	**7,292**	24,970
No less than 1 month but less than 3 months past due	**5,790**	60,121
No less than 3 months but less than 12 months past due	**111,890**	136,445
No less than 1 year past due	**306,725**	280,853
	615,166	779,238

The Group normally grants an average credit period of 30 to 90 days to its trade customers.

12 TRADE AND OTHER RECEIVABLES (continued)

(b) Impairment of trade receivables and bills receivable

Impairment loss in respect of trade receivables and bills receivable is recorded using an allowance account unless the Group is satisfied that recovery of the amount is remote, in which case the impairment loss is written off against trade receivables and bills receivable directly.

The movement in the allowance for doubtful debts during the period/year, including both specific loss components, is as follows:

	30 June 2010 RMB'000	31 December 2009 RMB'000
At 1 January	**124,669**	1,405
Provision for impairment losses	**681**	123,264
Written off of provision for impairment losses	**(5)**	—
At 30 June/31 December (note 12)	**125,345**	124,669

The individually impaired receivables relate to customers that are in financial difficulties and management assesses the recoverability is remote. Consequently, specific allowances for doubtful debts were recognised. The Group does not hold any collateral over these balances.

(c) Trade receivables that are not impaired

Receivables that were neither past due nor impaired (disclosed as current on the table given in note 12(a)) relate to a wide range of customers for whom there was no recent history of default.

Receivables that were past due but not impaired (as shown in the table in note 12(a)) relate to a number of independent customers that have a good track record with the Group. Based on past experience, management believes that no impairment allowance is necessary in respect of these balances as there has been no history of default and the balances are still considered fully recoverable. The Group does not hold any collateral over these balances.

13 OTHER FINANCIAL ASSETS

As at 30 June 2010, the Group had two contracts of principal-protected structural deposits with a commercial bank. The contracts had maturity periods of 7 and 14 days respectively. Both contracts have been fully settled subsequent to 30 June 2010.

14 PLEDGED BANK DEPOSITS

Bank deposits have been pledged to banks as security for certain banking facilities (see notes 15 and 16).

15 INTEREST-BEARING BORROWINGS

The interest-bearing borrowings were secured as follows:

	30 June 2010 RMB'000	31 December 2009 RMB'000
Secured	**14,261**	14,339
Unsecured	**893,582**	1,284,141
Total	**907,843**	1,298,480

The interest-bearing borrowings were repayable as follows:

	30 June 2010 RMB'000	31 December 2009 RMB'000
Within 1 year	**805,466**	1,046,090
After 1 year but within 2 years	**100,000**	250,000
After 2 years but within 5 years	**2,377**	2,390
Total	**907,843**	1,298,480

The interest-bearing borrowings as at 30 June 2010 amounted to RMB14,261,000 (31 December 2009: RMB14,339,000) are secured by the equipment and inventories with an aggregate carrying value of RMB237,555,000 (31 December 2009: RMB214,451,000).

The interest-bearing borrowings at 30 June 2010 bear interest at 0.68% to 6.50% per annum (31 December 2009: 2.55% to 6.50% per annum).

Certain banking facilities of the Group are subject to the fulfilment of covenants relating to certain of the Group's profitability and financial positions. If the Group breaches the covenants, the drawn down facilities would become payable on demand. The Group regularly monitors its compliance with these covenants. As at 30 June 2010 and 31 December 2009, none of the covenants relating to drawn down facilities had been breached.

16 TRADE AND OTHER PAYABLES

	30 June 2010 RMB'000	31 December 2009 RMB'000
Trade payables	**416,707**	413,060
Bills payable	**53,180**	104,442
Receipts in advance	**246,594**	316,444
Other payables	**76,158**	140,078
	792,639	974,024

Bills payable as at 30 June 2010 and at 31 December 2009 were secured by pledged bank deposits (see note 14). All of the trade and other payables are expected to be settled or recognised as income within one year or are repayable on demand.

An ageing analysis of the trade and bills payable based on the invoice date is as follows:

	30 June 2010 RMB'000	31 December 2009 RMB'000
Within 3 months	**208,708**	235,754
3 months to 6 months	**66,200**	98,020
6 months to 1 year	**50,594**	51,061
Over 1 year	**144,385**	132,667
	469,887	517,502

17 CAPITAL, RESERVES AND DIVIDENDS

(a) Issuance of ordinary shares

579,300 ordinary shares were issued as a result of the exercise of vested options arising from the Share Option Scheme granted to key management and employees (2009: Nil). Options were exercised at an average price of HK$1.71 per option. All issued shares are fully paid.

(b) Reserves

(i) Surplus reserve

Pursuant to applicable PRC regulations, PRC entity is required to appropriate 10% of its profit-after-tax (after offsetting prior year losses) to the reserve until such reserve reaches 50% of the registered capital. The transfer to the reserve must be made before distribution of dividends to shareholders. The surplus reserve can be utilised, upon approval by the relevant authorities, to offset accumulated losses or to increase registered capital of the PRC subsidiaries, provided that the balance after such issue is not less than 50% of its registered capital.

(ii) Exchange reserve

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of operations outside the PRC.

(iii) Other reserve

The other reserve of the Group comprises the difference between the nominal value of share of the subsidiaries acquired over the nominal value of the shares issued by the Company in exchange, the difference between acquisitions of non-controlling interests and entities under common control over the consideration given and the contribution of technology licenses by shareholder.

(iv) Capital reserve

Capital reserve represents the value of employee services in respect of share options granted under the Pre-IPO Option Scheme and Share Option Scheme and waiver of debts by the immediate holding company.

17 CAPITAL, RESERVES AND DIVIDENDS (continued)

(b) Reserves (continued)

(v) Share premium

The application of the share premium account is governed by the Companies Law (Revised) of the Cayman Islands. The fund in the share premium account of the Company is distributable to the shareholders of the Company provided that immediately following the date on which the dividend is proposed to be distributed, the Company will be in a position to pay off its debts as they fall due in the ordinary course of business.

(c) Dividends

Dividends payable to equity shareholders attributable to the previous financial year, approved and paid during the interim period

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
Final dividend in respect of the previous financial year, approved during the following interim period, of HK$Nil cents per share (six months ended 30 June 2009: HK$6 cents per share)	**–**	170,371

18 COMMITMENTS

(a) Capital commitments

Capital commitments outstanding at 30 June 2010 not provided for in the interim financial report were as follows:

	30 June 2010 RMB'000	31 December 2009 RMB'000
Contracted for	**99,611**	108,507
Authorised but not contracted for	**1,893,154**	1,874,335
	1,992,765	1,982,842

(b) Operating lease commitments

At 30 June 2010, the total future minimum payments under non-cancellable operating leases are payable as follows:

	30 June 2010 RMB'000	31 December 2009 RMB'000
Within 1 year	**2,919**	2,749
After 1 year but within 5 years	**5,346**	4,908
After 5 years	**9,283**	10,580
	17,548	18,237

The Group is the lessee in respect of a number of properties held under operating leases. The leases typically run for an initial period of one to fifteen years. None of the leases includes contingent rentals.

19 MATERIAL RELATED PARTY TRANSACTIONS

In addition to the related party information disclosed elsewhere in the interim financial report, the Group entered into the following material related party transactions.

(a) During the period, the directors are of the view that the following companies are related parties of the Group:

Name of party	Relationship
Guanghan Hongtai Business Trading Co. Ltd. ("Hongtai Company") (廣漢市宏泰商貿有限公司)	Hongtai Company is a party which spouses of certain directors and management have equity interest.
NCE Management, LLC	NCE Management, LLC is a party which certain management of Honghua America have equity interest.
Luzhou City Jianming Decorating Design Company ("Luzhou Jianming Company") (瀘州劍鳴裝飾設計有限公司)	Luzhou Jianming Company is a party which the brother of the spouse of a director of a subsidiary is the legal representative.
Guanghan Huite Fluid Appendix Co. Ltd. ("Guanghan Huite Company") (廣漢市惠特液壓附件有限公司)	Guanghan Huite Company is a party which the brother of a director of a subsidiary has equity interest.
Chengdu Juzhong Technology Co., Ltd. ("Chengdu Juzhong Company") (成都巨中科技有限公司)	Chengdu Juzhong Company is a party which the brother-in-law and brother-in-law's wife of a director of a subsidiary have equity interest.
Egyptian Petroleum HH Rigs Manufacturing Co. S.A.E. ("HH Egyptian Company")	HH Egyptian Company is 50% owned by Honghua Holdings.
Honghua-Ukraine Limited	Honghua-Ukraine Limited is 50% owned by Honghua Holdings.

19 MATERIAL RELATED PARTY TRANSACTIONS (continued)

(a) During the period, the directors are of the view that the following companies are related parties of the Group: (continued)

Particulars of significant transactions between the Group and the above related parties during the relevant period are as follows:

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
Purchases of parts and components		
— Hongtai Company	**3,761**	7,999
— Chengdu Juzhong Company	**445**	118
	4,206	8,117
Decoration service received		
— Luzhou Jianming Company	**50**	277
Sub-contracting services received		
— Guanghan Huite Company	**121**	714
	171	991
Sale of drilling rigs, parts and components		
— HH Egyptian Company	**502**	5,676

The directors of the Company are of the opinion that the above related party transactions were conducted on normal commercial terms and in the ordinary course of business.

(b) Balances with related parties

The balances with related parties are unsecured, interest-fee and have no fixed repayment terms. There was no provision made against these amounts at 30 June 2010 (31 December 2009: Nil).

19 MATERIAL RELATED PARTY TRANSACTIONS (continued)

(c) Key management personnel remuneration

Remuneration for key management personnel of the Group, including amounts paid to the Company's directors is as follows:

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
Basic salaries, allowances and other benefits in kind	**2,250**	2,117
Contributions to defined contribution retirement scheme	**48**	38
Discretionary bonuses	**—**	18
Share-based payments	**4,437**	6,340
	6,735	8,513

Total remuneration is included in "staff costs" (see note 6(b)).

20 CONTINGENT LIABILITIES

Dispute with natural persons

As of 31 December 2005, 728 employees of Oil Drilling Plant (the "original investors"), through 11 representatives, held collectively, 33.63% of Honghua Company's share capital. These 11 representatives were registered as shareholders of Honghua Company with the competent PRC government authority. On 7 January 2006, Honghua Company passed a shareholders' resolution to reduce its registered capital and buy-out equity interests from these 11 registered shareholders.

Honghua Company entered into a share purchase agreement with the 11 registered shareholders on 12 January 2006, under which, with the written consent of the 11 registered shareholders, it agreed to pay the share purchase price directly to the 728 original investors. The capital reduction process with the competent PRC government authority was completed on 26 April 2006. 664 of the 728 original investors have agreed to the buy-out arrangement and had accepted payment from Honghua Company. The remaining 64 investors, who, collectively, invested RMB651,385, claimed that they were still shareholders and refused to accept the buy-out arrangement and payment from Honghua Company.

20 CONTINGENT LIABILITIES (continued)

Dispute with natural persons (continued)

On 11 December 2007, 57 out of the 64 initiated legal proceedings at the Intermediate Peoples' Court of Chengdu City, Sichuan Province (Action No: (2008) Cheng Min Chu Zi No.53). The 57 individuals joined as plaintiffs to the legal proceedings against Honghua Company as the 1st defendant, Honghua Holdings as the 2nd defendant and 14 individuals including Shi Shuming (3rd defendant); Huang Dequan (4th defendant), Li Yan (5th defendant), Wang Yaoxin (6th defendant), Zhou Tao (7th defendant), Wang Wei (8th defendant), Chen Zhenghua (9th defendant), Yang Xuefeng (10th defendant), Yang Yuanchun (11th defendant), Ni Xiurong (12th defendant), Yu Zhenghua (13th defendant), Xing Manrong (14th defendant), Zhi Rongmu (15th defendant) and Liu Chuanjun (16th defendant) as the 3rd to 16th defendants. There are a total of 16 defendants.

The relief sought by the 57 plaintiffs include:

(1) An adjudication by the court that the 592,250 shares held by the 3rd to 16th defendants were actually owned by the 57 plaintiffs, and all the benefits and rights in such equity interests be restored to the 57 plaintiffs and the names of the 57 plaintiffs be entered into the register of members of Honghua Company;

(2) An adjudication by the court that Honghua Company be ordered to pay to the 57 plaintiffs a total sum of RMB296,125, being the 2003 dividends;

(3) An adjudication that the repurchase of the 592,250 shares of Honghua Company be declared null and void;

(4) An adjudication that Honghua Holdings be jointly and severally liable for the above members sought by the 57 plaintiffs and the consequential liabilities thereof, and that Honghua Holdings with Honghua Company be ordered to apply to the relevant Administration of Commerce to register the 57 plaintiffs as shareholders of Honghua Company; and

(5) An adjudication that all the defendants be jointly liable for the legal costs arising from proceedings.

On 13 March 2008, Honghua Company received the Supplemental Statement on Amending, Adding and Waiving the Statement of Claims (the "Supplemental Statement") submitted by the 57 plaintiffs. The plaintiffs added the following new claims:

(a) An adjudication that the 1st defendant, 3rd to 16th defendants be jointly liable for the damages of shareholders' right and interests, calculated until the date when the judgment is executed in full, including shareholders' rights for 3,760,379 bonus shares calculated until 30 September 2007, pre-emptive rights, and dividend from 2004 to 2006 in a total amount of RMB1,510,237.50;

20 CONTINGENT LIABILITIES (continued)

Dispute with natural persons (continued)

(b) An adjudication that the 1st defendant, 3rd to 16th defendants be jointly liable for the damages and costs of RMB228,000 incurred by the plaintiffs arising from these legal proceedings; and

(c) An adjudication that the merger and acquisition of Honghua Company by Honghua Holdings be declared null and void and that Honghua Holdings be jointly liable for all the claims against Honghua Company and other defendants.

Ally Giant, Ample Chance, Wealth Afflux Limited, Mowbray Worldwide Limited, Ecotech Enterprises Corporation, Otama Company Limited, Vast & Fast Corporation, Cavendish Global Corporation, Airtech Investments Limited, Ally Smooth Investments Limited, Charm Moral International Limited, Beauty Clear Holding Limited, Brondesbury Enterprises Limited, Oriental Starz Limited, Tech Express Enterprises Inc, Dobson Global Inc, Darius Enterprises Limited, Believe Power International Limited, Benefit Way International Limited, Birdview Limited and the existing shareholders of the company have executed a deed of indemnity in respect of dispute and risk dated 15 February 2008 in favour of the group under which they agree to jointly and severally indemnify any members of the group for any potential damages that the company may suffer as a result of the legal proceedings initiated by the 57 plaintiffs.

On 17 July 2008, another 2 individuals, Wu Chuan and Gong Yumei refused to accept the buy-out arrangement and payment from Honghua Company. The relief sought is the same as the 57 plaintiffs as mentioned above.

The legal proceedings have been completed on 19 June 2009 and the verdict is yet to be announced up to the date of these financial statements.

The directors, based on the PRC legal advisor's opinion, considered that these 64 original investors had never been properly registered as shareholders of Honghua Company with the competent PRC government authority, there is no legal basis under the PRC law for them to be regarded as shareholders of Honghua Company, and the directors consider that sufficient provision in legal costs in respect of the dispute has been made.

On 29 March 2010, one of the 64 investors accepted the buy-out arrangement and payment from Honghua Company, who is not a plaintiff to the legal proceedings against Honghua Company.

Definitions

"Ally Smooth"	Ally Smooth Investments Limited (聯順投資有限公司), a company incorporated in BVI with limited liability on July 5, 2006
"Ample Chance"	Ample Chance International Limited (宏機國際有限公司), a company incorporated in BVI with limited liability on July 13, 2006
"Articles of Association"	the Articles of Association of the Company, approved at extraordinary shareholders' meetings of the Company on January 21, 2008, revised and approved at Annual General Meeting of the Company on June 3, 2009
"Beauty Clear"	Beauty Clear Holdings Limited (俊朗控股有限公司), a company incorporated in BVI with limited liability on July 21, 2006
"Believe Power"	Believe Power International Limited (信力國際有限公司), a company incorporated in BVI with limited liability on July 21, 2006
"Benefit Way"	Benefit Way International Limited (益通國際有限公司), a company incorporated in BVI with limited liability on July 7, 2006
"Board of Directors" or "Board"	the Board of Directors of the Company
"BVI"	the British Virgin Islands
"Cayman Companies Law"	the Companies Law (2009 Revision) of the Cayman Islands
"Charm Moral"	Charm Moral International Limited (德美國際有限公司), a company incorporated in BVI with limited liability on July 18, 2006
"CNOOC"	China National Offshore Oil Corporation (中國海洋石油總公司), a state-owned enterprise established in the PRC on February 15, 1982
"CNOOC Group"	CNOOC and its subsidiaries
"Companies Ordinance"	the Companies Ordinance (Chapter 32 of the Laws of Hong Kong)

Definitions

"Company" or "our Company"	Honghua Group Limited, (宏華集團有限公司) an exempted company incorporated in the Cayman Islands with limited liability on June 15, 2007
"Concert Group"	several shareholders of Honghua Company forming a concert group as set out in the "Company History and Reorganisation-Ownership Continuity and Control" section of the Prospectus dated 25 February, 2008, namely, Zhang Mi (張弭), Ren Jie (任杰), Liu Zhi (劉智), Zheng Yong (鄭勇), Zuo Huixian (左輝先), Zhang Xu (張旭), Wang Jiangyang (王江陽), Chen Jun (陳俊), Fan Bing (范兵), Zhang Yanyong (張彥永), Ao Pei (敖沛), Tian Diyong (田弟勇), Shen Dingjian (沈定建), Liu Xuetian (劉學田) (deceased), Zhou Bing (周兵), Lv Lan (呂蘭), Tian Yu (田雨), Li Hanqiang (李漢強), Liu Yingguo (劉映國), Liu Lulu (劉露璐), He Guangfu (何光福), Zhang Zongyou (張宗友) and Chen Zongliang (陳宗良), out of which He Guangfu (何光福), Zhang Zongyou (張宗友) and Chen Zongliang (陳宗良) transferred an aggregate of approximately 9.1325% equity interests in Honghua Company to the other members of the Concert Group. The transfers were completed on February 17, 2006
"Controlling Shareholder(s)"	has the meaning ascribed thereto under the Listing Rules being, for the time being, Ally Giant, Ample Chance, Ally Smooth, Charm Moral, Beauty Clear, Believe Power, Benefit Way, Wealth Afflux Limited, Mowbray Worldwide Limited, Ecotech Enterprises Corporation, Vast & Fast Corporation, Cavendish Global Corporation, Brondesbury Enterprises Limited, Dobson Global Inc, Darius Enterprises Limited, Zhang Mi (張弭), Ren Jie (任杰), Liu Zhi (劉智), Zheng Yong (鄭勇), Zuo Huixian (左輝先), Zhang Xu (張旭), Wang Jiangyang (王江陽), Chen Jun (陳俊), Fan Bing (范兵), Zhang Yanyong (張彥永), Ao Pei (敖沛), Tian Diyong (田弟勇), Shen Dingjian (沈定建), Liu Xuetian (劉學田) (deceased), Zhou Bing (周兵), Lv Lan (呂蘭), Tian Yu (田雨), Li Hanqiang (李漢強), Liu Yingguo (劉映國) and Liu Lulu (劉露璐). Contracts executed by the Controlling Shareholders after Liu Xuetian's death were executed by his legal successors
"COOS"	China Ocean Oilfields Services (Hong Kong) Limited (中國近海石油服務（香港）有限公司), a company incorporated in Hong Kong with limited liability on April 2, 1982
"Director(s)"	member(s) of the Board of Directors of the Company

Definitions

"Golden Coast Company"	Honghua Golden Coast Equipment FZE (宏華金海岸設備有限公司), formerly known as Golden Coast Equipment FZE (金海岸設備公司), a company incorporated in the United Arab Emirates with limited liability on November 28, 2006 and a wholly-owned subsidiary of Honghua International
"Group" or "we" or "us"	the Company and its subsidiaries, and, for the period before the Company became the holding company for such subsidiaries, the entities which carried on the business of the Group
"HH Egyptian Company"	Egyptian Petroleum HH Rigs Manufacturing Co. S.A.E., a company incorporated in Egypt with limited liability on April 24, 2007 and is held by Honghua Holdings, Petroleum Projects and Technical Consultation Company, Engineering for the Petroleum and Process Industries Company and Tharwa Petroleum Company as to 50%, 25%, 10% and 15% respectively
"HK$" or "HK dollars"	Hong Kong dollars, the lawful currency of Hong Kong
"Honghua America"	Honghua America, LLC, formerly known as New Continental Equipment Co., LLC and as New Continental Equipment Co., Ltd, a limited partnership formed in the State of Texas on October 11, 2004, and converted into a limited liability company on December 19, 2006, and a 80%-owned subsidiary of Honghua Company
"Honghua Company"	Sichuan Honghua Petroleum Equipment Co., Ltd. (四川宏華石油設備有限公司), formerly known as Chuanyou Guanghan Honghua Co., Ltd. (川油廣漢宏華有限公司), a limited liability company established in the PRC on December 31, 1997, and a wholly-owned subsidiary of Honghua Holdings
"Honghua Holdings"	Honghua Holdings Limited (宏華控股有限公司), formerly known as Asia Harbour International Limited (宏海國際有限公司), a company incorporated in Hong Kong with limited liability on July 8, 2006 and a wholly-owned subsidiary of the Company
"Honghua International"	Honghua International Co., Ltd. (四川宏華國際科貿有限公司), formerly known as Sichuan Honghua Trading Co., Ltd. (四川宏華貿易有限公司), a limited liability company established in the PRC on January 13, 2004, and an 85%-owned subsidiary of Honghua Company
"Hong Kong" or "HK"	the Hong Kong Special Administrative Region of the PRC

Definitions

"Hongtai Company"	Guanghan Hongtai Business Trading Co., Ltd (廣漢市宏泰商貿有限公司), a limited liability company established in the PRC on June 21, 2002
"Hongtian Company"	Chengdu Hongtian Electronic Drive Engineering Co., Ltd. (成都宏天電傳工程有限公司), a limited liability company established in the PRC on June 6, 2001, and an 80%-owned subsidiary of Honghua Company
"Listing Rules"	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (as amended from time to time)
"Nabors Global"	Nabors Global Holdings Limited, an exempted company organized under the laws of Bermuda on February 25, 2005
"Nabors Group"	Nabors Industries and its subsidiaries
"Nabors Industries"	Nabors Industries Ltd., an exempted company organized under the laws of Bermuda on December 11, 2001, whose shares are listed on the New York Stock Exchange
"Nabors International"	Nabors Drilling International II Limited, an exempted company organized under the laws of Bermuda on March 12, 2003
"Nabors Management"	Nabors International Management Limited, an exempted company organized under the laws of Bermuda on December 23, 2004
"PRC" or "China"	the People's Republic of China and, except where the context requires and only for the purpose of this Interim Report, references in this Interim Report to the PRC or China do not apply to Taiwan or Hong Kong and Macau Special Administrative Regions
"RMB" or "Renminbi"	Renminbi, the lawful currency of the PRC
"Russia"	The Russian Federation
"Securities and Futures Commission" or "SFC"	the Securities and Futures Commission of Hong Kong
"SFO"	the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)

Definitions

"Share(s)"	ordinary shares issued by the Company, with a nominal value of HK$0.10 each
"Shareholder(s)"	holder(s) of our Share(s)
"sq.m."	square meters
"Stock Exchange"	The Stock Exchange of Hong Kong Limited
"Substantial Shareholder(s)"	has the meaning ascribed to it under the Listing Rules
"UAE"	the United Arab Emirates
"United States", "USA" or "U.S."	the United States of America, including its territories and possessions
"US$" or "U.S. dollars" or "USD"	United States dollars, the lawful currency of the United States
"Youxin Company"	Sichuan Honghua Youxin Petroleum Machinery Co., Ltd. (四川宏華友信石油機械有限公司), formerly known as Guanghan Youxin Co., Ltd. (廣漢市友信有限責任公司), a limited liability company established in the PRC on August 7, 1998, and an 80%-owned subsidiary of Honghua Company

HONG HUA

HONGHUA GROUP LIMITED

宏華集團有限公司